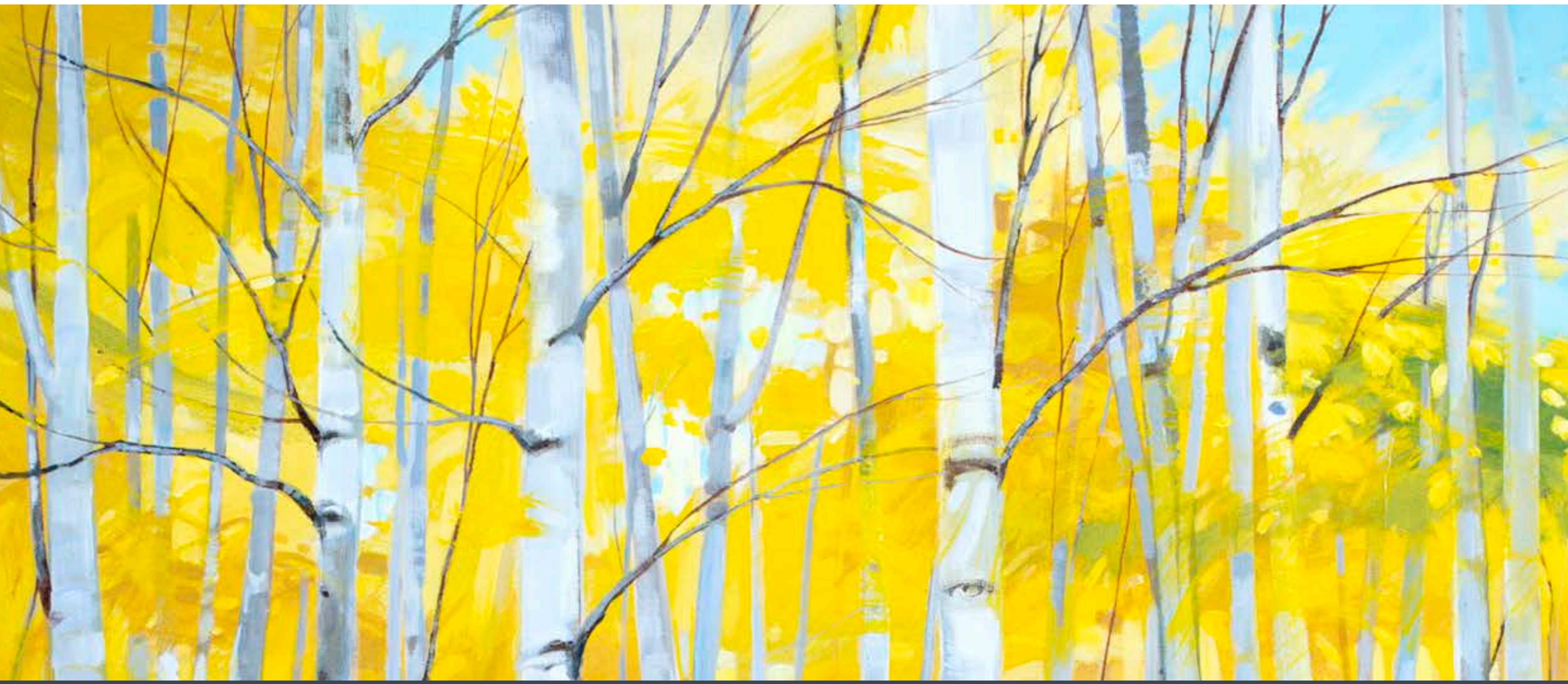
Perspective

Investment Management



Portfolio Manager Fund Commentaries

Balanced Fund

Perspective
Investment Management

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Balanced Fund Commentaries

Since Inception

August 2020

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October 2017

"What exactly makes us confident about owning an asset and grouping of assets for the next five to ten years?"

If we cannot convince ourselves with clear evidenced answers, our decision will be not to take action, do more work and thinking or wait for a sensible entry price. Resisting the temptation to act, doing the hard work, taking enough time to think and applying extreme patience are valuable resources in the investment decision making field. We design and structure our firm to focus on these, relentlessly.

A combination of these specific things that make us confident about long-term ownership are (a) paying a price that gives you the opportunity to earn meaningfully positive investment returns after inflation and costs, (b) competent and honest management, (c) an awesome underlying business and (d) delivering at or ahead of realistic expectations over time.

As of the end of October we had invested 35% of your fund in a diversified selection of JSE listed equities that we are confident about owning on a long-term basis.

Discovery is currently one of our largest investment positions in equity and a great example of the sort of asset that we search for, dream about owning and will purchase when all our criteria for long-term ownership are met.

A significant sell-off in SA government bonds following the budget speech gave us the opportunity to invest 5% of your fund in the 10-year bond at a price that can deliver an investment return after inflation of over 3%. In bond-speak, this is good value.

Please note that whenever we mention an individual investment, be mindful that it is meant as an example of the way we think about and manage your money.

Our work continues...

November 2017

"Who are the leaders of the firms we invested in?"

Adrian Gore. Johnny Copelyn. Johan Burger. Jannie Durandt. Adriaan de Lange. Graham O'Connor. David Munro. Bruce Hemphill. Norbert Sasse. Louwtjie Nel.

These ten people are the CEO's of the top equity holdings in our portfolio. They are qualified and experienced and have spent many years in their industries, and in almost every case in the companies they currently serve as leaders. They are an average age of 53 that offers the right mix of experience and energy with which to make key decisions that will influence the firms they lead - long after they depart the scene. We like that they are ambitious with credible plans communicated clearly.

We know and respect that people matter a great deal and therefore our evaluation of leadership plays a critical part in our research and portfolio management decision making. South Africa is blessed with a talented pool of executive leaders that increasingly have an impact all over the world.

Price matters, but to long-term investors people matter even more. We want to invest in companies led by amazing people.

Our work continues...

December 2017

A key element of our investment approach is to own businesses that can recognise and adapt to change. This means that we don't need to spend valuable time and energy forecasting changes, because we own businesses that can handle change; in fact, many of them have proven that they can thrive on change.

In our fund, businesses like Discovery, Remgro, HCI and Omnia have successfully handled significant changes, both positive and negative, in their respective histories. Where they have made mistakes they owned up to and learned from it, retained such knowledge and put it to good use. Best in class is when we observe that companies like Remgro and Omnia successfully transfer knowledge across multiple generations of leadership.

We spend almost all our time focused on assessing the current realities of a selection of businesses that we either own or will invest in when the price is right. We try to accurately and objectively observe 'what is', not what anyone wants or needs it to be.

Our research process is never-ending because businesses are not static entities operating in a vacuum. Any business of any size in any sector of the economy and anywhere in the world deals daily with a form of 'change' management - from the smallest to the most significant. Change represents opportunity and risk, and the best businesses in the world recognize and respond rapidly to either. Our research process is complex because it involves gathering information from and interactions with a diverse range of data and people, while we try to figure out (a) whether conclusions can be formed, and (b) whether they actually matter or not.

It is too early for us to conclude whether or not the election of Mr. Cyril Ramaphosa to the presidency of the ANC signals a turnaround in South Africa's trajectory. For now we reason that the likelihood of meaningful positive change has increased. Such a positive change, if it occurs, will present opportunities and risks to the businesses we own and we are confident that they will handle it.

Our work continues...

January 2018

Our Balanced Fund currently owns a healthy amount of cash. An interesting thing about cash is that, when the prices of other assets go up, cash is boring and looks old-school, but when the prices of other assets start falling, cash is the investor's best friend and looks absolutely amazing.

Our investment approach positions the fund according to the best investment opportunities presented by the markets at any point in time. Put bluntly; when we find lots of great long-term investment opportunities - being great businesses, led by great people, priced attractively - you can expect that the fund will have as little cash as possible. When great investment opportunities are scarce, the fund will have lots of cash. There is nothing 'magical' about this approach. It just makes common sense to us. We believe that it also makes common sense to our co-investors.

During the past 18 months, as we established our research universe and positioned this fund, it became clear to us that our list of great long-term investment opportunities is not extensive.

One of the cornerstones of the Perspective business and investment approach, patience, was therefore appropriate. Most of the equities and bonds of the wonderful companies that we would love to own one day are overvalued.

It is true that the share prices of many companies on the JSE have declined meaningfully over the past 6 months. Other than the assets we have already acquired, nothing else fitting our criteria has reached our buying levels. Yet.

Our work continues...

February 2018

In the 6 months since fund inception we have:
a.) **bought** into the shares of 23 JSE listed businesses with 43% of the fund,
b.) **sold** completely out of 1 of those 23 businesses for 0.8% of the fund,
c.) **bought** into SA Government 10-year Bonds with 5% of the fund,
d.) **bought** into UK Pounds with 4.5% of the fund.

We told you that we are long-term investors. There is a reliable and readily understandable number that we will report at least annually that evidences whether or not we walk our talk; 'portfolio turnover on an annualised basis'. The basic calculation is Total Asset Sales / Total Fund Assets. The resulting number is a measure of how active we are in the fund and can be used to accurately infer the investment time horisons we are applying.

Should this number consistently be 100% or more, it means we executed loads of transactions that resulted in our fund owning its assets for less than a year. That would serve to disqualify us as long-term investors. Should this number consistently be 20% or less, it means our fund owned its assets for 5 years or longer, meeting our definition of long-term investing.

Our portfolio turnover works out to 1.6%. Put bluntly, other than the relatively small sale of a single security, we've barely touched the portfolio. We are doing what we told you we would. Keeping asset transaction costs inside the fund low is an often overlooked but important contributor to your eventually realised bottom-line investment returns.

You will receive the first Semi-Annual Reportback Letter shortly. In this letter we hold ourselves to account and we set out a more detailed overview of our investment process, portfolio management actions, fund positioning and our observations on realistic future investment return expectations.

Our work continues...

March 2018

During the past 7 months, 15 of the 23 businesses held in our portfolio disclosed significant new developments, over and above financial results.

Good businesses and business environments are dynamic, so it is normal that so many of the businesses in our fund warrant attention to significant new developments. On some of these, such as Investec's leadership changes, we were able to formulate our opinions reasonably quickly; we like it. On the other hand, Sanlam's recent investment of approximately R12bn for a controlling 53% stake in Moroccan based Saham Finances, will take us more time to comprehensively analyse, understand and appreciate, before formulating an opinion.

Our work continues...

April 2018

We're all for digitalisation, but in a faster and easier world one often overlooks the intangible value of seeing a physical certificate of ownership of an asset and receiving a regular cash dividend or bond coupon payment. The value lies in recognising and being reminded that we are in fact a part-owner of a real business functioning in the real world.

Please do not think of our investments as numbers flashing past on a ticker tape or lines on a chart. This is impossible when one pays too much attention to daily price movements and headlines.

We have been investors in Exxaro since our fund's inception in September 2017. At first glance, it appears that the share price has not increased by much, which is accurate. However, in just under 8 months Exxaro has paid us a year-end dividend of R3.20 plus a handsome special dividend of R12.55 per share. From a total return perspective, Exxaro has been a solid investment to date in our fund and we are able to reinvest these dividends.

Our long-term investment philosophy enables us to partake in the receipt of dividends and bond coupons for many years to come.

Our work continues...

May 2018

At the end of September 2017, we owned the shares of 17 businesses totalling 33% of our fund. Our research led us to conclude that a generally overvalued market environment at that point in time warranted a conservative positioning.

In the past 6 months the Johannesburg Stock Exchange Index declined by a seemingly benign 6%. However, an important and lesser known perspective is that 111 of our investable universe of 209 companies in South Africa declined by an average of 20%. Forty-two of these declined by an average of 38%.

With this information as backdrop, we have steadily increased our fund's exposure to equities whenever businesses met our four key long-term investment criteria - understandability, trustworthiness, valuation and liquidity.

It is therefore pleasing to share with you that we now own the shares of 25 businesses totaling 47% of our fund. These additions improved the fund's future investment return expectations. Furthermore, it improved the fund's diversification and robustness in terms of business sectors, industries and geographies, as we acquired excellent businesses like Sasol, Sappi, Anglogold and British American Tobacco with significant operations outside South Africa.

As promised, we remain discerning in our evaluation of new investment ideas. For example, we have only bought 3 of the 42 companies mentioned in the 2nd paragraph above. The rest of them continue failing one or more of our four key long-term investment criteria.

Our work continues...

June 2018

Our portfolio strategy resulted in our fund being invested in a selection of mid to large sized businesses with strong balance sheets and other defensive qualities like diversified revenue streams and superb management that can recognise and adapt to change.

Buying underperforming stocks exposed to an economic downturn and a contraction in government, corporate or consumer spending during a time of generally fair valued to expensive stock markets is a recipe for catching falling knives. Furthermore, a falling knife can quickly turn into a burning house when these companies have excessive debt levels and are smaller companies, when they can also suffer from debtholder or lender distress and forced selling by large shareholders. We want to continue avoiding such companies.

Significant renewed uncertainties in South Africa coupled with global concerns about trade wars is busy shaping a market environment that we expect will provide us with a range of attractive new investment opportunities during the next 12-18 months.

We closely monitor our wish-list of excellent businesses that we look forward to acquiring on a long-term basis. They meet all our other criteria, except they're not cheap enough yet. These share prices on average have declined by over a fifth, but as a group they remain overvalued. Most of these have some ways to go south before we will be able to invest in them.

The completion of our fund's first full year is at the end of August, when we will be sending a review of our individual portfolio holdings in the annual letter to all our investors.

Our work continues...

July 2018

This month we delve into Perspective's definition of what makes a business 'Quality' in our approach to investing your savings.

To us, quality is an intangible attribute. It is a mindset in an individual, or it can be labeled an attitude. In a business context it is called a culture, or in more practical terms, it is just the way things are done.

We focus on searching for, investing in and spending almost all our time and energy on learning more about businesses with the intangible quality attributes that we respect and admire.

A few examples of the types of quality attributes we consider important are:

- An ability to see the wood for the trees.
- An ability to accept reality.
- An ability to adapt to reality.

We give preference to businesses with engrained attitudes that became part of the DNA of the organisation itself. This means it stands above any individuals in the business, including its leaders, and it transcends multiple generations of its people.

Businesses that possess these intangible quality attributes we seek cannot easily be placed into a neat little black & white box. It turned out, once we identified what we were looking for and we looked hard, they could be found in any country, business sector or industry and they can be of any size.

Bringing it all together, in the final reckoning, these intangible quality attributes must become tangible by delivering meaningful long-term growth in per share real-world business values. We will only believe a business meets our definition of quality once we can evidence it.

Our work continues...

August 2018

We are often asked what we really mean by 'long-term'. It is one of our most important differentiators as an investment firm, so we enjoy describing how we think about and do things on a long-term basis.

Starting with our business philosophy, we live it in terms of being "cradle-to-cradle", meaning we designed and built every aspect of our firm with a purpose to create enduring value for multiple generations of your and our families. That's right; your and our children's children's children's… etc.

Ending with our investment philosophy, we prefer to measure and show you the facts. In our February 2018 monthly portfolio manager commentary, we disclosed our annualised portfolio turnover level of 1.6%, representing how (in)active we were in transacting fund assets on your behalf in the first 6 months. The end of August 2018 represents 1 year of managing your savings and our updated annual portfolio turnover level came in at 6.1%. This compares extremely favourably with the average of all global unit trusts, which credible sources inform us is running well over 100%.

Our low annual portfolio turnover evidences we continue doing as we promised to as long-term investors on your behalf. It may spike somewhat in an individual year, but you can expect our annual portfolio turnover level to average no more than 20% over rolling 5-year periods. The lower the better, because that would imply (1) we owned better quality assets for longer than 5 years, and / or (2) we made relatively fewer mistakes in our research assessments.

A research study by a respected global investment industry leader concluded annual fund costs increase by approximately 1% for each 100% of annual portfolio turnover. This finding is further supported by our own experience and calculations. Our low turnover gives you a cost advantage that will become increasingly significant over time.

In late September you will receive our Annual Letter to Investors where we will share more detail about the assets and businesses in the fund with you. We trust you will enjoy reading it.

Our work continues…

September 2018

We can send you eloquent stories about our outlook and convictions of the market environment and how we are positioned all we like, but what really matters is how our portfolio as a whole reacts when the markets get really tough. September was a pretty decent proxy for a really tough market, with the JSE index declining by 6% and the Rand strengthening. At one point, just a few days before the end of the month, the JSE was down over 10% for the month.

Our portfolio took this in its stride, with the fund down 2.3% in September. This is an example of what we really mean when we talk about the 'robustness' of our portfolio and its individual building blocks.

What helped us the most was our continued significant holding in cash, and bonds. Cash is an often misunderstood and under-appreciated asset class, but it truly comes into its own when a month like September - and indeed the past 13 months - rolls around.

When markets are generally overvalued cash is our default and represents an eminently sensible active investment idea in the fund.

Upon closer investigation all is not well with offshore stocks. Our work clearly shows the growing discrepancy over the past 6 months between the positive 5.8% return (in US Dollars) of the MSCI World Index and the *minus* 5.4% return of the average global stock in our database of over 12,000 global companies. This is particularly noticeable in smaller companies, which declined by a sobering 11%. This week we invested in our first directly listed offshore business, but in global markets investments that meet our criteria remain few and far between at this time.

Our portfolio strategy remains to safely get us all to the point where the fund will be fully invested in a diversified selection of quality understandable businesses led by trustworthy people priced for delivering attractive future growth; with at best more money than you invested alongside us and our families, and at worst flat to only slightly down in a market meltdown scenario when many others would have lost serious money and may quite possibly be tempted to panic.

Our work continues...

October 2018

The JSE Allshare Index *declined* 6% in October on the heels of September's 5% *decline*, while the MSCI World Index *declined* 7.4% in October.

Against this backdrop, we are pleased that the fund continues to behave robustly, *declining* by just 0.9% in October. Over the past 12 months the fund is *up* 4.4%, while the JSE Allshare Index *declined* 7.9%.

We are, for the most part, satisfied with fundamental progress at the assets already in the fund. We are also starting to find a few more investment ideas that meet our strict requirements.

Despite being dated November 8th, this particular fund fact sheet misrepresents the current reality to some extent, because this past week we invested in 5 businesses directly listed offshore. We would like you to know what is going on in the fund and what you are buying into, should you invest additional amounts or if you are one of our new investors.

As of this writing, our directly held offshore assets amount to 12.3% of the fund, of which 4.8% (of the fund) is in UK Pounds, with the rest invested in 6 truly outstanding businesses. Each of them are world leaders in their respective industries, with global scale and diversification. As with everything else we invest in, we intend owning them for 5 to 10 years or longer.

Our investment team members spent the past 3 years filtering and carefully assessing both South African and offshore investments. The real reason that we have not bought direct offshore stocks until recently, is that they were not cheap enough.

Stepping back a bit and taken as a whole, the fund remains conservatively positioned with 49% in a diversified selection of equities. We see absolutely no reason to get over-excited at this point and prematurely charge into overvalued markets with all our valuable reserves.

Our work continues…

November 2018

Everyone in our firm and a number of our direct family-members invest in this fund in the same fee-class as our investors. This results in an important alignment of interest. Not only do we care deeply about the investment decisions we make, but we also care deeply about getting and keeping fund costs as fair and reasonable as possible; for everyone.

We took notice when the Total Expense Ratio (TER) measured over the fund's first 12 months worked out to 1.67%. We have confirmation that the actual TER is running at 1,32%, of which 0.15% is VAT.

We looked into this together with our fund administrators, Prescient Fund Services. We found the current TER to be significantly overstated due to the way the standard industry calculation penalises a fund in its first few months. In short, we concluded all our investors are in fact paying a fair and reasonable fee - as per our commitment.
We take this sort of thing seriously and it was formally reviewed at Perspective's board meeting in November.

Just so you know, if we found evidence that pointed to us having charged you an excessive fee, we would have offered you a reduction in portfolio management fees to make up for it.

We anticipate the TER to reflect reality from early on in the new year.

For those of our investors that may be interested in the finer technical details of expense ratio calculations, you are more than welcome to contact any of us and we will gladly share the maths and explain.

We wish you and your loved ones a joyful, relaxing and safe festive season and a prosperous 2019.

Our work continues...

December 2018

December offers opportunity for reflection, partly because a year has passed, but mostly because it is quieter.

2018 will be marked down by most as a tough year in the investment markets. Being conservatively positioned and not losing serious money was critical. Global equities were hit hard recently with for example the S&P 500 Index declining by a significant 15% between December 1st and the 26th.

On the other end of the risk spectrum, the quoted prices of crypto-currencies were decimated. Fortunately, these instruments fell far outside our key investment criteria of understandability and trustworthiness. We continue steering well clear of them.

We are pleased to have steadily increased the equity component of our fund from the 35% invested in 17 businesses in September 2017 to the current 45% invested in 31 businesses. What's more, taken as a group, they are now offering increased diversification across industries and geographies as well as far more attractive investment return expectations.

We believe it is reasonable for us to expect the currency and investment markets in the first half of 2019 to remain volatile, especially given the local elections in South Africa and clarification of the ANC's intended land expropriation amendment to the constitution. We welcome volatility, because it usually leads to investment opportunities for patient, disciplined long-term investors.

Our portfolio management strategy remains to navigate these market conditions on your behalf in order to get all of us safely to the point where the fund can be more fully invested.

Our work continues...

January 2019

Occasionally we observe substantial dislocations between underlying weakening economic reality and strong asset prices in the markets.

These dislocations can continue for years for reasons we cannot see or understand. And then, out of the blue, they can change course, without warning but with painful consequences.

In 2016 when we established Perspective the empirical evidence led us to conclude that the average South African consumer was facing an unusually rough patch. Basic living expenses had been growing much faster than incomes, while jobs were either disappearing, being disrupted or uncertain. At the same time, the consumer's investments – mostly pension funds and property - were flat to negative, while net debt remained at elevated levels.

This trend continues today, the economy is weak and interest rates are relatively low, thereby making these consumers vulnerable to further job losses and interest rate hikes. Most data points we regularly evaluate provide continued support for this conclusion.

We ask the question, why do South African retail stocks remain stubbornly overpriced?

Disappointing trading updates and substantial share price declines from the likes of Mr Price, Truworths, Massmart, Woolworths and Shoprite indicate the past 6 months have been far weaker than expected. We think this provides a more sober temperature reading of the current reality facing the average South African consumer. The closing of the dislocation we spoke of in our opening paragraphs is in full swing and we are paying close attention.

We remain discerning and cautious about investing in the South African retail industry at this point in the cycle.

Our exposure to this industry remains negligible as of this writing.

Our work continues...

February 2019

The S&P 500 index ended last year *down* by 4.4% to post its first negative total return since 2008. Since the start of this year that market is *up* by 12%. The VIX, which is an index used to measure market volatility, declined by almost 55% since the middle of December to the end of February. This suggests that investors are a lot less nervous today than they were a mere 3 months ago. The sheer magnitude of these swings highlights just how unpredictable global equity markets are in the current environment.

The global economy is under pressure. US inflation reported at 1.6% for January is the lowest since 2016. The threat of higher US interest rates which spooked the market in December has all but disappeared. Growth in Europe and China is also lower and slower than what markets seem to be pricing in at this stage of the economic cycle. We don't spend any time trying to predict how the cycle will play out. We do, however, spend a meaningful amount of time trying to understand where companies are positioned in the cycle and how they are most likely to perform in especially turbulent markets.

Our unwavering commitment to clients is to maximize returns by taking the lowest possible risk. The best way we know how to do this is by maintaining a long-term focus and paying attention to the things that really matter. Paying too much attention to prices going up or down in choppy markets is likely to detract from the long-term ability of fund holdings to compound wealth for clients over time. We remain cautious of putting money to work in global equities where expected returns are still below the level we would require from the perspective of a Rand-based investor. The currently underweight fund position in global equities is an outcome of that work.

We will be sharing our current fund holdings as well as a full review of our investment strategy in confidence with existing clients via email over the next week. We trust you will enjoy reading this and welcome any thoughts, views and opinions you may have.

Our work continues…

March 2019

Moody's sent a team to review and update their view on South Africa during the last week of the month. The rating agency decided not to take any action. They appear to be providing a window for a Ramaphosa-led ANC government to evidence their political commitment to much-needed structural reforms after the national elections in May. It is a reprieve which keeps the country's sovereign credit rating at investment grade with stable outlook – for now. Moody's are effectively deferring judgement until the next review in November 2019.

As custodians of clients' life savings, we have a responsibility to review the companies we choose to invest in on a more regular basis than rating agencies. We reviewed all of the fund holdings during the first quarter of the year and specifically looked for leading indicators of distress or anything that could potentially derail the underlying investment theses. Confidence levels increased in companies like MTN and Sasol, while a combination of excessively leveraged balance sheets, industry structure and management concerns resulted in us exiting positions in Tongaat Hulett, Mediclinic and British American Tobacco.

Risk management is an explicit part of our investment approach. What often goes unseen is the companies we choose to not invest in. We have deliberately avoided putting money to work in companies like PPC, Brait, Aspen and Nampak, despite what appears to be relatively attractive prices. These companies have taken on high levels of debt at the top of the economic cycle to fund aggressive acquisitions and projects in complex operating environments. The fund has also maintained a relatively small position in listed property, which is substantially cheaper than what it was a year ago, but continues to trade at prices which understate the risks at the broader industry level.

Our work continues...

April 2019

South Africa heads to the election booths on 8 May with voters getting to cast their ballots for the party that best represents their interests. The consensus expectation is that a Cyril Ramaphosa led-ANC will retain leadership of the country. Interim polls suggest that control of the major metropolitan cities will be relatively more evenly contested between the ANC, DA and EFF.

Elections should be about accountability – *Have elected public servants done what they said they would do?* They tend to play out somewhat differently as campaigns are positioned to somehow defer that accountability to some unknown time in the future and shift attention towards some new story to soothe public discontent. The 5-year period between voting cycles also provides a convenient window to manipulate the ebb and flow of voter sentiment.

An important part of our investment process is not to allow political stories to obscure economic reality. Periods of political uncertainty often provide incredible opportunities for truly long-term investors. Our interest is piqued when expectations of extreme political outcomes are priced into markets. Companies led by trustworthy, appropriately incentivised people, that just happen to be priced for excessively bad political outcomes, are especially good candidates for inclusion in actively managed portfolios. The ability to change our minds and vote against people found to be less accountable than they ought to be is a particularly important part of protecting clients capital.

Our work continues…

May 2019

Global markets succumbed to the *"Sell in May and go away"* theme that tends to perennially see investors being net sellers of listed equities over the month. The US S&P 500 declined by around 6.6% with all major European and Asian equity indices also falling by at least 5% in US Dollars. The sell-off was partially blamed on the resurfacing of geopolitical risks and further escalation of global trade tensions.

The evidence suggests that equity markets are continuing to price in exceedingly good outcomes at a point in time when bad outcomes are likely to happen more often than not. Our investment process is designed to look at the full global opportunity set and only allocate capital when understandable businesses are available at what we consider to be fair prices. The current domestic cash exposure of approximately 45% is an outcome of that process. Under existing market conditions, it just so happens that Rand-based cash is a relatively sensible investment idea in its own right with returns of around 7.3% versus domestic equity returns of 2.4% over the last 12 months.

We are not forced buyers of any assets. The flexibility of a balanced fund in combination with a truly long-term orientation allows us to be somewhat more discerning when investing client capital. The fund is currently priced to deliver returns in excess of inflation + 5% over the next 5 years. Having the optionality of higher cash exposure to unlock further value for clients is something we are particularly excited about.

Our work continues…

June 2019

The JSE All-Share index returned around 4.8% for the month to reverse the negative return of approximately the same amount during the market selloff in May. Resource stocks lead the rebound with a monthly return of 10.1%. There was also some much-needed respite for the Rand which strengthened against all major developed market currencies and was almost 4% up against the US Dollar.

At the global index level, equity, bond and property markets are all exceedingly expensive. The US S&P 500, Dow and Nasdaq are trading at *all-time* highs with aggregate corporate bond and real estate indices also priced at historically elevated levels. July 2019 also marks the longest running US economic expansion on record at 121 months. Europe is experiencing the peculiarity of *negative* nominal government bond yields, which means that investors are actually paying governments to hold their money. The value of global negative yielding government bond debt is now a staggering $13 Trillion – again the highest level in history.

These anomalies are further evidence of investors taking on increasingly higher levels of risk to generate what we consider to be below par returns. After reviewing market conditions over the first half of the year we are seeing further evidence to support our cautiously opportunistic approach. The companies which meet our minimum investment criteria are still trading on the expensive side of what we would consider a fair price, but we are slowly uncovering more ideas which improve the expected return profile of the fund without compromising portfolio robustness.

Our work continues…

July 2019

The JSE All-Share Index (ALSI) ended the month down by 2.4% with broad-based selling across most sectors. Resources and Financials were particularly hard hit with both indices falling by more than 5%. Sentiment towards South Africa appears to have turned especially negative. Foreign investors were net sellers of approximately R14bn of SA equities. The bond market was also not spared with outflows of R11bn continuing the trend of R16.7bn outflows in June.

Continued interest from longer term foreign investors provides a contrasting perspective. PepsiCo announced a R24bn offer for Pioneer Foods at a sizable 55% premium to the share price. The US-based food and beverage business is the third foreign company seeking control ownership of a JSE listed company following attempts by Israeli consortium MilCo to acquire Clover and Germany-based Aton's hostile pursuit of Murray and Roberts.

South Africa is not without its fair share of challenges. To quote the CEO of one of our investee companies "*This is definitely not a place for sissies*". Our commitment to clients remains to identify good companies lead by able and trustworthy people which happen to be priced for excessively bad outcomes. We tend to not pay too much attention to the movement of capital in listed stock or bonds markets. Our purpose is to think and act like long term owners of companies as opposed to short term renters of stocks. The willingness of control investors like PepsiCo, Aton, and Milco to allocate meaningful amounts of capital to South Africa further supports our current thinking that local assets are offering discerning long-term investors with relatively good value.

Our work continues…

August 2019

Increasing uncertainty in listed markets allowed us to increase fund holdings of both domestic and global equities over the last month.

Global markets appear to be taking direction from re-escalations of trade and currency wars, expectations of lower and slower growth, and a Brexit standoff which continues to defy logic. Throw in a certain president that tweets and communicates *too much* of his views and investors are justifiably nervous. Domestic concerns remain centred around touted state regulation in land ownership, healthcare, and pension funds. Throw in a president that probably communicates *too little* of his views and nervy investor sentiment is equally justified.

Our work continues to prioritise companies run by trustworthy people building their businesses on durable cultural values. They are sufficiently respectful towards minority investors and communicate in a clear, candid manner without compromising on the integrity of their founding principles. These attributes don't necessarily fit neatly into analyst valuation spreadsheets but are exactly what we pay attention to as truly long-term investors.

The companies we most want to own are by no means 'on sale' but some have started selling off to levels where they meaningfully improve the robustness of the portfolio. Our portfolio management process constantly looks to improve the balance between risk and return. By combining reasonably-priced *great* companies with cheaply-priced *good* companies the fund is positioned to earn higher returns at substantially lower risk than was the case at fund inception 2 years ago. The most exciting part is that we have in no way compromised on the integrity and character of the people we choose to partner with in *any* of these companies.

Our work continues...

September 2019

September 4th marked our fund's 2-year anniversary, so this is an opportune moment to briefly pause and reflect.

Since fund inception, being September 4th, 2017, the total return (including dividends) of the JSE AllShare Index is a *negative* 2%. That doesn't look too bad, but it hides the fact that the total return of the average JSE listed company is a *negative* 21%.

The average share price of relatively smaller sized companies and property stocks are *down* 33%, which we think qualifies in the 'serious decline' category. As an aside, so much for property being a safe haven.

Please brace yourself, because here is a scary fact. Of the 290 JSE listed equities & property stocks combined, 112 of them are down by more than 30%, at an average decline of 54%! That deserves an exclamation mark.

The biggest winners in the SA market over this timeframe have been few and far between and are highly concentrated in a few industries like platinum, iron ore, gold and unsecured lending. With the exception of gold, these industries are highly vulnerable to the increased risks of a global economic recession. Despite the hype, the objective truth is that platinum is *not* a precious metal.

It may not (yet) be reflected in the index itself, but this has been a tough market environment that rivals our own experiences in the market downturns of 1998, 2003, 2008 and 2015. We are therefore pleased and proud that our fund has in the first instance largely protected your capital. Simultaneously, we have slowly but surely become more fully invested in quality businesses, led by great people, at incredibly attractive price levels far below their real world business values. We achieved this without excessively trading in and out of assets; our annualised fund turnover over the first two years came in under 10% p.a.

We have owned a number of our fund holdings since inception and nothing pleases us more than receiving our dividends from them in cash every 6 months. It serves as a terrific regular reminder that we do not just own pieces of paper, but real businesses in the real world with thousands of real people creating value for their customers and thereby for us, daily.

Looking deep in the mirror at ourselves and our firm, we can confidently state that we have done exactly what we promised all our investors at the outset.

Our work continues…

October 2019

Finance minister, Tito Mboweni, delivered an especially gloomy Medium-Term Budget Policy Speech showing a sizeable debt hangover from years of wasteful government spending. To compound the country's woes, Moody's rounded out a rather sobering period when they changed the outlook on the sovereign credit rating from stable to negative.

The bad news is that South Africa is currently directly on the path towards a full downgrade to non-investment grade status next year. The good news is that the expectation of that downgrade has already largely been discounted by the market. The Rand actually *strengthened* after the Moody's announcement as the market expected the news to be much worse than it turned out to be.

The Funds positioning is an outcome of balancing the risks and opportunities of the good and the bad news. Recent portfolio actions include actively diversifying earnings away from South Africa – either by investing directly in sensibly priced offshore assets or indirectly through companies that happen to be listed on the JSE but earn a large percentage of their income outside the country. We also continue to maintain sufficiently high cash balances and liquidity in the fund to allow us to enter and exit positions as needed.

The political reality is that the country is at a tipping point. The economic reality is that the local investment universe offers long term investors the opportunity to invest in robust businesses at prices substantially below what we think they are worth. We continue to have a cautiously opportunistic outlook and have positioned the fund with both the political and economic realities of the country in mind.

Our work continues...

November 2019

An increasing number of South African listed companies and state-owned enterprises have been found wanting in terms of corporate governance. While we are sickened by the extent of many of the shenanigans we uncovered, we also take heart from the fact that the South African government and investment industry is slowly but surely mobilising to address these matters. We believe this is a very good thing for you as a long-term investor in this fund.

We have been and remain particularly wary of investing in any companies that rely heavily on doing business directly with the South African government from a governance standpoint, but also from a cash flow perspective.

We tend to identify our most serious governance concerns at two types of companies; firstly, at professionally owned & managed companies where executives have no significant skin in the game and are incentivised in an asymmetric fashion – heads they win but tails they win too.

Secondly, we tend to identify governance concerns at companies where untrustworthy control owners and other similar powerful vested interests are doing things at the expense of minority investors.

Our investment approach and commitments are crystal clear. We have never and will not knowingly invest in these types of companies under any circumstances. We do not care how much upside might be possible for short-term oriented speculators. We refuse to gamble with your money. It is clear to us this research 'attitude' of ours has directly contributed to helping us avoid the most harmful permanent losses of capital over the past few years.

We are constantly busy deepening our research and reviewing each of the businesses we own in the fund. It strikes us just how many of the ones we own currently have control owners with a long-term track record of protecting minority investors and executives with significant skin in the game.

We co-invest alongside you in this fund with all our own investable savings. We believe this represents the best form of skin in the game. This is the best way, some say the only way, to ensure we keep our focus where it matters most – on this fund and every aspect thereof that protects and enhances your and our long-term investment outcomes.

We would like to take this opportunity to for the third time wish you and your loved ones restful and safe year-ends. If you are coming to Cape Town, please feel free to stop by our offices in the city for a visit. We love meeting and learning more about and from you.

Our work continues…

December 2019

We woke up this morning, being January 3rd, to the shocking but perhaps not surprising news that the US carried out a drone airstrike in Iraq. The prices of oil and gold and their related listed stocks are up, while most everything else sells off. It is at times like these that we experience the value of holding assets in the fund such as Anglogold, Barrick Gold, Sasol and Transocean.

It is also at times like these that we experience the value of *not* holding significantly overvalued and consensus, widely owned assets.

In combination with our focus on investing in businesses with proven business models and exemplary owners & leaders, it provides the fund as a whole with an element of resilience we term 'robustness'. We feel it is important that the owners and leaders of our investee businesses, as well as our investors and ourselves, can be afforded the incredible luxury of staying calm and rationally focused on identifying and pursuing the best long-term opportunities during turbulent times in the economy and markets.

We continue with the portfolio management strategy we formulated in mid 2017. In a nutshell, the evidence points to this being a time to remain appropriately conservative and focused on capital preservation and long-term value. We search for sensible reasons to change our stance all of the time, but to date have identified no such reasons. Where assets met our core investment criteria we acted on a discerning and measured basis to invest therein, without relaxing any of our standards.

The Perspective team is excited about the fund and the ongoing development of our business and network. We are ready for and look forward to being of further value to you in 2020 and beyond.

We mostly interact and communicate with our investors in private and in confidence. Please feel free to stop by our offices in Cape Town or let any of us know if you wish to know more about anything we do here on your behalf.

Our work continues...

January 2020

Many people are currently uncertain and concerned about South Africa's leadership, political and economic reality and prospects. The CEO of a listed local business even has a specially made up word for this state of mind; "gatvolheid", loosely translated as 'having had it up to here'. As fellow citizens and parents, at Perspective we acknowledge and share in the substance of these concerns, while we continue working around the clock to try and make some sense of it all.

As investors we feel fortunate to have personally experienced and managed money through various points of material uncertainty and concern in the markets since 1992. In addition, several of our firm's stakeholders contribute their additional decades of market and business knowledge and insight. It is our considered view that the current levels of uncertainty and concern are no worse than we lived through in 1994-1995 (political change & recession), 1998-1999 (global emerging markets crisis), 2002-2003 (recession), 2008-2009 (global financial crisis), 2013-2014 (Southwestern European debt crisis) and 2015-2016 (commodities).

From our combined experiences, we know the greatest long-term investment bargains are always found in times of heightened uncertainty and even outright fear. This reality is unfolding in South Africa and is precisely what we are ready for. Contrary to a broadly held negative consensus, at Perspective we are excited about the assets we already own and those on our research priority list.

Buying and holding (1) understandable, good quality assets (2) owned and led by trustworthy people (3) when they are cheap is a sound investment approach, rooted in logic and evidence. When this investment approach is applied in a 100% committed and disciplined manner, it delivers satisfactory investment returns over rolling 5 to 7-year periods, equating to the length of a typical business and market cycle.

With our fund's track record extending over a period of 2 years and 5 months, it is still too early to judge investment outcomes over a full cycle. However, it is never too early to judge whether our investment actions are in line with our commitments to our investors. We are confident in stating we have done, and continue to do, that which we committed to.

Our work continues…

February 2020

February 2020 was a particularly tough month in local and global investment markets with meaningful declines in equity indices. Looking at the underlying index constituents – the thousands of companies that make up the market as a whole – it was significantly worse, as well as wide-spread across countries, sectors and industries.

As you can see from our negative February fund price change, we have clearly not fully escaped this, but our significant holding in cash and near-cash helped to soften the blow – as it was intended and expected to.

Media coverage and consensus appears centered on the negative economic and market impact of the Coronavirus. However, we feel the truth is the evidenced reality that at equity index levels markets are quite simply overvalued. That people need to find a story to help explain the times is as old as time. This is in the nature of investing and we feel it is important for us to both appreciate and respect this. Our point is that laying the blame for market declines at the door of the critically endangered and beautiful Pangolin could be a mistake.

Amid all this external noise our team continue to scrub annual reports and evaluate existing and new investment ideas. Most importantly, the incredible quality of our investor base and our ability and commitment to stay well under the radar gives us a firm bedrock from which to calmly go about deploying our fund cash into only the very best investment opportunities on your behalf. The volatility and declines in markets are dishing up increasingly attractive long-term investments in quality, scale businesses with strong balance sheets and free cash flows. The good news is there is no need to swing for the fences by buying a host of poor quality, sub-scale companies with poor balance sheets and free cash flows that are between unlikely and certain to be wiped out in an economic recession. We have slowly but surely been adding to our existing top-quality holdings and adding a few new ones.

Please know we remain as discerning as ever and we are under no pressure nor in a hurry to become fully invested. As and when top quality assets become available at increasingly attractive prices, we will buy into them in a disciplined manner.

You can expect to receive a letter from us soon with a more detailed reflection on our investment actions and outcomes over the past 2 ½ years, as well as our current fund positioning and investment outlook.

Our work continues…

March 2020

Right upfront we would like to acknowledge that the world has unexpectedly changed in many respects on a more or less permanent basis. Some impacts will of course be negative, but importantly, some will undoubtedly be positive. We have, in a patient and disciplined manner, spent a lot of time and effort thinking through this.

In these times of substantially increased volatility in the world and in stock markets, we responded in the following ways;

1. We substantially increased the regularity of our written non-public communication with fund investors, in order to keep you as fully informed as possible of economic and market developments, its impacts on the fund and our thinking, and the changes we made to the fund.
2. Our portfolio managers engaged and personally spoke with *every* investor in the fund in the past week.
3. Starting in November 2019, our investment team carefully re-assessed every single investment held in the fund. Where deemed necessary we significantly reduced or sold out of assets that we considered not robust enough to cope with such a severe economic shock as the global virus pandemic has resulted in.
4. We have been able to take advantage of above normal levels of volatility in the markets to even further improve the quality and cheapness of the diversified group of businesses we own in the fund.

With 61% in equity the fund remains far from being fully invested. This is appropriate given the investment opportunities we see at this time.

Our businesses typically have strongly capitalised family or corporate control owners, leaders who deeply understand & respect what stewardship means, strong balance sheets & free cash flows, and they deliver valuable goods and services their customers need on a daily basis. Our continued commitment to investors is to keep uncovering more of these and to patiently acquire them - provided they are cheap enough.

In addition, we increasingly notice our businesses buying back their own deeply undervalued shares and the directors buying shares for themselves, paid for in hard cash. These are encouraging signs of confidence and increased alignment with us as minority shareholders.

Most importantly, we trust you will keep safe and that you are surrounded with the people you care about most. As one of our investors recently told us, "...this is one humungous global exercise in humility". We agree strongly!

Our work continues...

April 2020

The level of financial gearing of any business in any industry is a key part of our assessment of what we term 'robustness'. It has held true for centuries that a highly geared business is almost certain to fail outright should almost any form of adversity befall it. We continually monitor all of the businesses in our fund for any signs of deterioration in their financial gearing. Whenever warranted we will act to reduce our exposure or sell out entirely.

It struck us many years ago that spending time and energy trying to predict and worrying about every single thing that might go wrong with each of our businesses is not productive. The truth is that life and business is dynamic and constantly in motion. Every respected business executive we have ever come across spends every day and night of the year figuring out new solutions to new puzzles. That is their job and we want them to get on with it.

Our approach is to *assume* the worst possible case occurred and to rather spend our time and energy trying to figure out whether or not our businesses could survive that worst case, and what it is exactly that would allow them to survive. Almost without fail, having a strong balance sheet or having a caring, responsible owner with a strong balance sheet is a key factor to surviving significant adversity.

We are confident that we have acquired a diversified portfolio of businesses that meet our criteria for 'robustness'. In times like these, with business failures on the rise globally and locally, owning a portfolio with staying power is simply not up for debate. When the economies and markets eventually recover, it is the survivors that will tend to emerge even stronger than before.

Our work continues…

May 2020

An important feature of the way we invest and manage investment risk is how our portfolio composition slowly shifts in terms of its exposure to equity and the concentration of its individual holdings in listed businesses.

All else being equal, when markets are generally more expensive, we should have a low total exposure to equity and small position sizes in individual listed businesses. As and when markets offer us better and more long-term investment opportunities, we should have a higher total exposure to equity as well as larger position sizes in individual listed businesses.

To illustrate, at inception in September 2017 we had 33,1% of the fund invested in equity. Our top 10 fund holdings added up to 22% of the fund, at an average of 2,2% invested in each individual holding. In contrast, at end May 2020 we had 62,8% of the fund invested in equity. Our top 10 fund holdings added up to 30,7% of the fund, at an average of just over 3% invested in each individual holding.

This transition in our equity exposure and concentration levels is (a) typically a slow process measured in *years* and (b) *entirely* dependent on the opportunity set available to us in the markets.

There is evidence of us having entered a part of the market cycle in South Africa where certain listed assets are sold at any price for reasons that have nothing to do with their underlying business fundamentals. This can result in spectacular dislocations between their traded prices and their real-world business values. We were prepared for this; we have participated in a few of these rare opportunities already and are closely monitoring the rest on our wish list.

Our work continues...

June 2020

The arbitrary month of June 2020 offers us a good reminder of how the slightest change in investor sentiment can result in large price changes of listed assets.

We know that good things tend to happen to undervalued, quality listed assets. That said, we openly acknowledge that we can never know *when* exactly these good things will unfold. For truly long-term investors, a lack of certainty on timing is not a serious problem.

It is a mathematical *certainty* that the total investment return over a 5-year period is exactly the same whether it occurs incrementally over time or happens all at once at the very end of that period.

Three key conditions are necessary to deliver meaningful investment returns over a full market cycle of 5 to 7 years:

1. **An abundance of undervalued, quality listed assets** – *only available when consensus investor sentiment is overwhelmingly negative.*
2. **Improving business fundamentals** – *policy certainty, growth in sales and profits, growth in per share business value.*
3. **A swing in consensus investor sentiment from negative to positive** – *usually, but not always, follows clear evidence of improved business fundamentals.*

As set out in our 2020 Annual Investor Letter, sent to you in June, we believe condition 1 has been met. There is also sufficient evidence for condition 2 to have been upgraded to a 'work in progress', specific to the individual businesses we own.

The order in which these 3 conditions are met is important. For example, rapidly rising share prices that lack evidenced improvements in business fundamentals represents a *weak*-form gain.

It is far more constructive when rapid share price gains in our businesses are supported by evidenced improvements in their business fundamentals.

Our work continues…

July 2020

Following on from our last fund comment, we evaluate new evidence daily in order to gauge fundamental progress at the businesses we own. Of course we want positive fundamental progress, as that is an important second step towards delivering strong future investment returns.

As of this writing, we own 41 individual businesses in the fund. It is pleasing that 18 of these are already evidencing positive fundamental progress.

An interesting observation about the way stock market prices behave is that prices often lag fundamental changes; both positive and negative. Popular, widely owned assets often defy gravity and their share prices stay high or travel sideways while their fundamentals clearly continue deteriorating.

The share prices of unpopular, uncrowded assets often stay low or travel sideways while their fundamentals clearly continue improving.

In both cases, one can never know precisely when the tipping point is reached, consensus investor sentiment shifts and the share price reflects the underlying fundamental reality. Sometimes the lag is short, measured in days, weeks or months. Other times the lag is long, measured in years.

As we have seen in the precious metals industry in the past 3 months, once the tipping point has been crossed price changes can be significant within surprisingly short periods of time.

There is one important exception, worth keeping in mind. The share prices of quality businesses rarely become deeply undervalued and usually do not remain so for very long. We suspect this happens because they are attractive acquisition candidates for trade competitors, control owners or company executives.

Our work continues...

An executive in our network once told us there is 'opportunity in chaos'. As long-term value investors, we wholeheartedly agree. We look for opportunities to acquire listed assets at prices well below their durable business values. However, occasionally we come across businesses that are owned and led by people that have demonstrated a clear understanding of how the stock market really works. They know how to take advantage of the market's ebb and flow to create *long-term growth in <u>per share</u> business value.*

Amid chaos, deeply undervalued assets present several opportunities for sensible executives. To be specific, they can (a) acquire and cancel their own undervalued listed shares, (b) acquire undervalued listed or unlisted competitors, (c) implement sustainable BEE structures, and (d) incentivize and align key staff members. They can also use the opportunity to acquire shares for themselves, thereby further aligning their personal interests with minority shareholders.

For unfathomable reasons, often beyond our immediate understanding, while many executives may speak with authority about this topic, few seem to act on it.

We are growing increasingly excited about our portfolio. We own deeply undervalued assets, but we are also observing concrete executive actions to create long-term growth in per share business value at a large and growing number of our businesses.

Italtile bought back shares and acquired a stake in Easy Life Kitchens. **Foschini** is buying Jet from Edcon. **Cashbuild** is buying The Building Company from Pepkor. **Adcock Ingram** bought Plush Leather Care. **Long4Life** and **Santova Logistics** bought back shares. **Afrimat** bought Coza Mining from Arcelor Mittal, and Unicorn Capital Partners from its minority shareholders. Across the portfolio quite a number of executives are buying shares for themselves, paid for in cash.

Our work continues...