Please note that the commentary is for the retail class of the fund.

The fund had a challenging first quarter, declining by 5.1%. The fund has performed well against both its peer group and the quantitative benchmarks over longer periods.

Our large weighting in global and, in particular, selected emerging market equities, significantly added to fund performance over the past year and quarter respectively. Three of the fund's largest international holdings, i.e. 58.com (+9%), Booking Holdings (+14%) and Vostok New Ventures (+9%) delivered strong performances. Vostok is a Swedish listed investment holding company that is focused on investing in early stage technology businesses that are run by entrepreneurs and typically benefit from strong network effects. Vostok's current investment portfolio is dominated by their 13.2% stake in Avito where they were one of the early investors. Today, Avito is the largest and most liquid online classifieds platform in Russia and dominates traffic in all the key high value classifieds verticals, namely autos, real estate and careers. The market opportunity for Avito remains immense and it has a long runway of growth ahead of it. Add to this a business model where long-term sustainable EBITDA margins of 60-70% are achievable, and it becomes clear why we would want to be shareholders in this business.

Overall, the JSE had a poor quarter, with the JSE All Share Capped Index declining 6.0% (and with it dragging down its rolling 12-month returns to 9.6%). The weakness was driven by industrials (-8%) and property (-20%), with the latter being impacted by the collapse in the share prices of the Resilient group of companies, i.e. Resilient (-65%), Fortress B (-46%) and Nepi Rockcastle (-44%). This was on the back of allegations of management impropriety principally related to share price manipulation. Fortunately, the fund had no exposure to these counters. The financial sector continued its rally post ANC elective conference with banks (+4.2%) and life insurers (+1.2%) ending the quarter in positive territory. The resources sector declined -3.8% with platinum stocks (-21%), in particular, having another terrible quarter. We have taken some profits from our offshore equity positions and we did add opportunistically to domestic stocks – thereby marginally increasing our domestic equity exposure.

We continue to maintain reasonable exposure to resources based on our assessment of their long-term value. Our preference for Anglo American (+10%) over BHP Billiton (-3%) – based on more attractive commodity mix and valuation – continued to contribute to performance for the quarter. However, our platinum exposure – mainly through Northam – has continued to be a detractor from performance.

The large mining companies have all recently reported results which were generally in line with, or better than, market expectations. The theme of strong cash flow, deleveraging and capital returns to shareholders continues. High prices, limited capital expenditure, benign mining inflation and low freight rates have led to the mining companies generating above normal free cash flow. We are starting to see mining inflation and capital expenditure levels pick up. In addition, growth is starting to make its way back into mining executives' vocabulary (examples include greenfields copper at Anglo American and coal acquisitions by Glencore). Our hope is that it remains measured and that these executives aren't lured into chasing growth at the expense of returns. News flow with respect to South African mining has also been distinctly more positive. Ramaphosa's election has brought much hope and optimism to the country. With his long history of involvement in the mining industry, the hope is that the sector's prospects improve. Indeed, one of Ramaphosa's first actions was to replace the mining minister. In addition, new leadership has been injected into Eskom. In early April, the South African High Court issued a declaratory order, effectively recognising the principle of 'once empowered, always empowered'. Legal recognition of this principle would remove the risk of ongoing dilution of ownership for equity holders. Our expectation is that increased policy certainty, a reduction in patronage and politically induced safety stoppages should go a long way to improve the operating environment for our local miners.

The British American Tobacco (BTI) share price declined by 16% during the quarter – partly on the back of sector rotation out of global staples and partly due to regulatory concerns around the threat of the US Food and Drug Administration's intention to reduce nicotine consumption. This is not the first (and certainly not the last) time that tobacco companies will face regulatory headwinds in their markets. However, we continue to believe that these concerns are overblown and that the market is underappreciating the pricing power, stable earnings and cash flow generation inherent in the business. Furthermore, we are optimistic on the earnings opportunity from next generation products and the synergies that could be extracted from the recently completed Reynolds deal. BTI is currently trading on a 13.4x one year forward P/E multiple and 10.4x our assessment of normal earnings. This is incredibly cheap for a globally diversified business of this quality and we continued to add to our BTI position during the quarter. The share is now the single largest position in the fund.

Although domestic banks have had a strong run since December, Investec has been a standout laggard due to the market's preference for banks with more exposure to domestic South Africa in anticipation of a strong economic recovery. With respect to Investec, in addition to its South African bank, one is also buying a high-quality asset and wealth management franchise as well as a UK banking operation where the earnings base is currently low (and where there is upside optionality should they be successful in pursuing their UK private banking aspirations). Investec is currently trading on less than a 10x one year forward P/E multiple, c.8x our assessment of normal earnings and also offering almost a 5% dividend yield. We think the valuation is very attractive and added to our position during the quarter.

The UK property sector appears to be coming back to life after the economic uncertainty surrounding Brexit. Initially sparked by the Hammerson all share offer for Intu in December, Hammerson ultimately became an acquisition target in March following the French-listed REIT, Klepierre's, proposed cash and scrip offer. Although Klepierre's proposal represented a c.40% premium to the undisturbed Hammerson share price just prior to the announcement, we still believe that at a c.20% discount to Hammerson's recently reported NAV, the potential offer significantly undervalues Hammerson's equity.

Material changes for the quarter included a further reduction in our Naspers position on the back of a very strong run in Tencent's share price. We also sold most of our position in Discovery – again on share price strength. We further exited our position in Foschini as the business was trading above our assessment of fair value. We currently have limited exposure to the South African clothing retailers given their stretched valuations. At this point our preferred domestic equity exposure are the defensive counters such as Netcare, Life Healthcare and the food retailers (i.e. Pick n Pay and Spar) where we think valuations are still attractive.

In this uncertain world, our objective remains on building diversified portfolios that can absorb unanticipated shocks. We will continue to focus on valuation and seek to take advantage of attractive opportunities that the market may present to us, and in so doing generate inflation-beating returns for our investors over the long term.

Portfolio managers
Karl Leinberger, Sarah-Jane Alexander and Adrian Zetler

as at 31 March 2018