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

The fund delivered a -4.0% return for the quarter, which was behind the benchmark return of -1%. While the short-term performance is disappointing, our aim is to deliver outperformance over longer-term time periods. To this end, the fund's returns since inception are compelling, with alpha of 3.7% per annum, net of fees.

Our key mining holdings (Anglo American, Exxaro, Northam) were positive contributors to performance this quarter. We have added to our holdings in Anglo American and BHP Billiton. BHP Billiton owns large, low-cost assets in iron-ore, copper, oil and coal. As a result of healthy commodity prices, combined with restrained capital expenditure (miners still bear the scars from the last down cycle), we expect BHP Billiton to generate meaningful free cash flow in the coming years. We expect a material portion of this will be returned to shareholders, along with the proceeds of their shale gas asset disposal.

For our non-mining rand hedges, Mondi continued its strong share price performance. We used the opportunity to reduce our position size, given the reduced margin of safety. We used the proceeds to buy other rand hedges whose share prices came under pressure, including Naspers and MTN.

Naspers' share price declined on the back of a pullback in the Tencent share price. Tencent's recent quarterly earnings were disappointing, and short-term earnings expectations have been revised downwards due to the restructuring of certain Chinese government departments and the subsequent delays in the licensing of new online games. Chinese authorities have also proposed new regulations around protecting minors from the adverse effects of online games, which has created uncertainty in the Chinese gaming sector. We believe the licensing delays to be a temporary disruption to the business. Furthermore, our interpretation of the new proposed gaming regulations for minors is that they will favour strong, responsible incumbents like Tencent. As such, we remain optimistic od the longer-term prospects for their online gaming business and are still very encouraged by the opportunities they have in growing their advertising, financial services and cloud businesses. In addition, Tencent has an outstanding investment portfolio, the value of which we believe is still very underappreciated by the market. In the case of Naspers itself, we are very encouraged by Naspers' management's actions around portfolio optimisation and the steps taken to reduce the discount to its underlying intrinsic value. In this regard, Naspers management announced that they would proceed with the unbundling of Multichoice.

The MTN share price declined after the surprise announcements from the Central Bank of Nigeria (CBN) and the Nigerian attorney general that MTN were in violation of certain foreign exchange control regulations and that they were demanding MTN to repatriate $8bn back to the country and pay an additional $2bn in back-taxes. These actions have created widespread uncertainty and is undermining the investment case for foreign investment in Nigeria. As the pressure of market forces has come to bear, the tone of more recent public announcements has been less aggressive and more constructive. It is our view that their claim has little merit. That said, even in a worst-case scenario with MTN Nigeria carried at zero value, we still see upside from current share price levels.

Domestically, things remain very tough. The South African economy dipped into recession with Q2 GDP of -0.7%, well below the consensus expectations of growth of +0.6%. Recent reporting by consumer-facing businesses reflects this, with numerous companies reporting results below expectations. In September, President Ramaphosa announced a new economic stimulus package which included a number of supply and demand side reforms aimed at both raising productivity and public sector-driven investment projects. These include infrastructure spend projects, easing of work and travel visa requirements, employment tax incentives and market friendly revisions to the Mining Charter 3. Despite these initiatives being a step in the right direction, the SA economy has many structural challenges and improvements are likely to take a long time to gain traction.

SA Inc shares have been under pressure, with the sell-off seeming indiscriminate between high-quality and low-quality businesses. As a result, we continue to own defensive, cash-generative businesses like Spar, Distell and Netcare. Local financial shares have fared much better. Our financials exposure is primarily via Standard Bank, Nedbank and Old Mutual. The latter two performed well over the quarter. We materially reduced our Old Mutual holding – placing the proceeds into Nedbank, Quilter and the rand hedge stocks discussed earlier.

The external environment is very challenging. The amplitude of daily stock price moves we have been seeing is unnervingly large, with the potential for the euphoria or pain that accompanies them. We strive to ignore this and remain commited to our disciplined, valuation-driven approach to stock-picking and portfolio construction. The volatility we see provides opportunities to the patient, long-term investor. Given current valuations of the stocks we own, we are excited about prospective returns for the fund going forward.

Portfolio managers
Neville Chester and Pallavi Ambekar
as at 30 September 2018