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

The fund returned 2.1% during the third quarter of 2019, slightly behind the 2.8% return of the MSCI Emerging Markets Index (both in rand terms). The cumulative performance for 2019 remains very pleasing, at 25.9%, which is 14.2% ahead of the index return of 11.7%. Over one year, the fund has returned 14.3% (9.5% alpha) and, over three years, 9.1% p.a. (-0.4% p.a. alpha). Although we are very pleased with these strong short-term returns, the long-term nature of the fund makes longer-term returns more meaningful for assessment. In this respect, while the five-year return is behind the benchmark (-1.9% p.a. alpha), the seven-year (0.3% p.a. alpha), 10-year (0.3% p.a. alpha) and since inception figures (1.8% p.a. alpha) are all pleasingly positive.

The largest positive relative contributor to the fund during the quarter was New Oriental Education (New Oriental). The share was up by 21.7% in rand terms during the quarter after delivering positive full-year7 results (their financial year end is 31 May) and reinforcing the guidance that margins will improve in the years ahead as their heavy investment in new capacity starts to mature. New Oriental currently earns operating margins of 12%, well below the 18% they used to earn three years ago before they started investing heavily to grow their capacity, which has since doubled. Members of our team met with management in Beijing in August and our positive long-term view on potential was reinforced – the margins on mature operations exceed 20% and unsuccessful sites can be fairly easily shut down if they are not meeting expectations. Were the business to stop growing today, the ramp-up of their already-opened learning centres (which are not fully contributing to revenues), combined with the increase in margins that accompanies this (they are incurring the full cost of employing teachers and paying rent), could see profits double within three years. This is in addition to the substantial organic opportunities available to New Oriental, whose market share is still in the single digits, despite being the largest operator of on-site after-school tutoring facilities in the country. New Oriental contributed 0.5% of alpha during the quarter; however, the strong share price performance did reduce the relative attractiveness of the share and we reduced New Oriental from a 3.0% position to 2.3% as a result.

The second-largest relative contributor was Wuliangye Yibin (Wuliangye), the Chinese baijiu spirits brand. Up by 13.3% in rand terms, Wuliangye contributed alpha of 0.4% to the fund. Over the quarter, one of our analysts visited the company at its headquarters in mainland China for the second time this year, a visit that reinforced the positive steps the company is taking to improve its pricing ladder and increase the share of premium baijiu within its portfolio. Over the last year, Wuliangye has returned 98.9% and has contributed 2.53% to the relative performance of the fund. It remains a top 10 position in the fund despite this strong performance, as we believe it is a unique asset, capable of compounding earnings at 20% p.a. for the next few years, and this is not yet reflected in the share price.

Other meaningful contributors during the period were British American Tobacco (+13.5% return for 0.37% alpha), Brazilian education company Estácio (23.2% return for 0.36% alpha) and global brewer Anheuser-Busch InBev (+16.2% return for 0.21% alpha). The big news in the tobacco industry was the aborted merger attempt between Philip Morris International (PMI) and Altria. As PMI shareholders (2.6% of fund), we were vehemently opposed to the deal and communicated this strongly through a letter to the board immediately upon announcement of the merger talks. The market's reaction to the deal (PMI fell as much as 9% on the day of the announcement) clearly sent the same message to the affected parties. We were against the deal for a variety of reasons, not least of which is the very negative regulatory environment for combustible cigarettes in the US currently, to which PMI would have been exposed through Altria's US operations. Furthermore, Altria's shareholding in electronic cigarette company Juul is problematic as Juul is a potential competitor to PMI's well-received Heat-Not-Burn (HNB) IQOS product, which will be launched in the US shortly (by Altria, with a royalty payable to PMI). Juul has come under significant regulatory scrutiny due to the prevalence of teenage vaping, which itself has been partly driven by the dubious marketing tactics and an array of flavours that give the impression that vaping is harmless. We believe IQOS has tremendous long-term potential in many markets (it has been very successful in Japan, Korea and parts of Europe already) as a means of reducing the consumption of far more harmful combustible cigarettes. We did not want any exposure to Juul, so, as PMI shareholders, the failure of the merger talks was, in our view, a very positive development.

On a less positive note, the biggest detractor for the quarter was Chinese classifieds business 58.com, which fell 14.9% for a -0.85% impact. The two biggest "verticals" within 58.com are property and jobs (blue collar), both of which are (in theory) affected by the broader macroeconomic slowdown being experienced in China. Trade war fears have intensified negative perceptions of stocks exposed to the broader economy and, with 58.com viewed in this light, it has fallen for reasons of sentiment rather than fundamentals. Toward the end of the quarter, 58.com fell significantly after a competitor Meituan Dianping (Meituan) (a new fund holding, which we discuss in more detail lower down) moved into the blue-collar jobs market. One cannot dismiss this development, given Meituan's disruption of other internet-based platforms; however, in our view, Meituan's jobs platform is more suited toward matching users of its delivery services with advertisers in the restaurant and service industry. This is a specialist niche within the broader market and, we believe, is unlikely to materially impact on 58.com's appeal for jobs postings. 58.com's EBITDA margins (mid-20%s) are below most peers in other countries, despite earning similar gross margins. Over time, as the business continues to scale up and investment declines, profits should grow at a rate materially higher than revenue growth. 58.com continues to deliver operationally, with revenue up 21% and operating profit up 24% in the first half results to end of June 2019. It now trades on a 12% free cash flow yield (to enterprise value), which is very attractive in our view, and so it remains one of the largest positions in the fund.

Company	Axel Springer	Ebay	Naspers	Adevinta	Scout24	Schibsted	Recruit	Zillow
Ticker	SPR.DE	EBAY	NPNJO	ADEB.OL	G24.DE	SCHA.OL	6098.T	Z
Classified Revenues (USD in MM)	1,347	1,022	875	661	591	315	3,081 (HR Technology)	1,281
							6,799 (Media & Solutions)	
Classifieds EBITDA/Adj. EBITDA	40%	45-55%(2)	46%(3)	25%	55%	45%(4)	15%	19%
							24%	

Source: 58.com Investor Relations

Other big detractors for the quarter were the relative underweight in Taiwan Semiconductor Company, which returned 26.8% in the quarter and cost the fund 0.49% in relative performance. Chinese wealth manager Noah Holdings declined by 24.9% in the quarter and the 1.23% position (at the start of the quarter) therefore cost the fund 0.35% in relative performance. The ongoing political strife in Hong Kong weighed heavily on Hong Kong-listed life insurance group AIA, which fell 5.5% and cost 0.28% in relative performance. AIA generates about 40% of new business in Hong Kong and it is estimated that half of this comes from mainland China. In addition, 30% of new business is originated directly in China. Although it was only a small detractor in the quarter (0.21% negative contribution), the fund's Ctrip holding was also negatively affected by China/Hong Kong developments, as travel bookings are a large part of its business, and China-to-Hong Kong travel makes up around 30% of outbound ticketing volumes processed by Ctrip. The fund's other baijiu holding - Jiangsu Yanghe - fell by 11.9% to cost the fund 0.27% in relative performance.

There were several new buys in the fund, the largest of which was Meituan, mentioned above. Meituan is a platform business offering food delivery services (such as Uber Eats), hotel booking and in-store services such as restaurant bookings, movie tickets and hairdressers (to name but a few examples). Meituan has a number one or two position in its various business niches and leverages its massive scale to gain a cost advantage over weaker peers. In food delivery, it competes primarily with Alibaba-backed Ele.me, while in hotel bookings it has surpassed Ctrip in the lower end of the market (when measured by room nights, but not by revenue, since Ctrip targets mid- to higher-end hotels). Online penetration in most categories remains quite low, so there is still substantial room from the market leaders to take share from offline over time, which will further enhance their cost advantage over time.

Another new buy was Indian online travel agency (OTA) Make My Trip. We have met this business several times over the years and believed it had significant potential, as it has many similarities to Ctrip, which has been in the fund for some time. The Indian market is, however, several years behind China's. India is also a far more cost-conscious market with lower per capita incomes. The airline industry is dominated by low-cost carriers and the hotel industry is also focused mostly on lower-tier hotels. Travel is still predominantly domestic and for leisure, which is more price sensitive. With more than half of air tickets still booked offline and perhaps 80% of hotels booked offline, the runway for online to take share from offline is significant, and Make My Trip already has more than 50% market share in the online space after acquiring the second-largest OTA in India (Ibibo). The relatively faster growth of the non-air ticketing part of the business in recent years has resulted in air ticketing revenues making up only a third of revenue from more than 50% a few years ago. In addition to airline tickets and hotels, Make My Trip offers a variety of value-add services such as train ticket bookings (the state-run railways in India are not easy to book online), car hire, full package holidays, travel insurance and assistance with procuring visas. As these higher value-add services grow in the mix, we believe Make My Trip's profitability will be significantly enhanced, as it is currently loss making. Naspers was previously the largest shareholder in Make My Trip, followed by Ctrip, but a recent shareholding structure change has resulted in Ctrip becoming the largest shareholder, with Naspers becoming a material shareholder in Ctrip. We believe that Make My Trip will benefit from having a dedicated OTA as its largest shareholder, since Ctrip has been through a similar development and learning curve in China.

Another new buy in India was Axis Bank, the third-largest private bank in the country. We have previously highlighted the investment case in the private banks in that country as they take market share from the poorly run public sector banks in what is still a fast-growing market overall. Axis is a previous fund holding that we sold when it started to approach our assessment of fair value. Like many of its peers that grew too fast, the book quality deteriorated and some time was needed to clean up the bad debts. A highly regarded new CEO was brought in and the share price recovered strongly. Axis is increasingly becoming a more retail-focused bank, which, in our view, is significantly more attractive than focusing on corporate loans, which are more competitive and can have a bigger negative impact on the book (as we have seen in the bank and its peers historically). More recently, the (relative) slowdown in the Indian economy, the liquidity issues within the banking sector as a whole and the aggressive provisioning of old loans under the new CEO saw the Axis share price decline by around 20% (in rupees) from its second-quarter peak. At these levels, we believe Axis offered significant upside and we started to build a small position toward the end of the third quarter. As the bank is growing quite fast it also needed to raise capital, and we were able to purchase most of the position during this capital raise at a discount to the prevailing market price. Subsequent to purchasing the position, the Indian government reduced corporate tax rates, which will be positive for shareholders of Axis and shareholders of some of the fund's other Indian pure domestic holdings, like HDFC and HDFC Bank.

The last new buy was a repurchase of Turkish discount retailer BIM, one of the best-performing businesses anywhere in the world over the last two decades. We had sold out of BIM in mid-2018 due to the economic crisis in Turkey and a loss of confidence in the country's government, which looked to be operating in an increasingly populist and haphazard fashion. BIM has continued to grow its store network through all of this and has gained share by limiting price increases in an environment of very high inflation within the Turkish economy. The Turkish lira, which was one of the worst-performing currencies in 2017-2018, has stabilised, and with interest rates and inflation declining, we believe that BIM will continue to deliver high returns on capital in an improving economy in the years ahead.

Two small positions were sold to zero in the quarter – Global Mediacom in Indonesia (we still retain a small position in free-to-air TV operator Media Nusantara, which is majority owned by Global Mediacom) and bank holding company Itaúsa in Brazil. Members of the team travelled extensively during the quarter, meeting management of over 100 companies in various locations as well as conducting site visits to holdings in Russia, China, Hong Kong and Macau. The travel will continue in the fourth quarter, including a visit to Brazil, whose weight in the fund has declined to 6.8% - the lowest it has been in several years.

Portfolio managers
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as at 30 September 2019