

A high-speed photograph of water splashing against a black background. Several gold coins are visible, some partially submerged and others floating on the surface, creating a dynamic and energetic scene.

OLDMUTUAL

FUNDAMENTALS

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Quarter 1



INVESTMENT GROUP



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A MESSAGE FROM THE MD

KHAYA GOBODO

LEAVING OUR MARK IN CHANGING THE WORLD

Conversations about the kind of world we want to live and raise our kids in are becoming increasingly more frequent and intense across the spectrum of social interaction. For us as an investment business, we care deeply about conscientiously allocating capital in ways and in areas that will result in a positive impact for all stakeholders, beyond our promise to pursue excellent return outcomes for our clients. This is Impact Investing for a sustainable future and is a growing movement across the globe. Once a movement like this gains critical mass, it can change the world and at that point, it becomes an unstoppable force that is self-propelling. As we and other large corporates and institutions continue to staple our credentials to this movement, it will continue to grow and have a real tangible impact on the trajectory we are currently on.

On the other side of the coin is another growing movement which is gaining a lot of traction amongst individuals. Individual consumers are increasingly aware of where they buy their goods and services; they care about the core values of organisations they choose to work for and, as we have recently seen, they are protesting and demanding action on climate change. Twenty years ago, this was not the case. We are already seeing evidence of this movement converging with the movement around Impact Investing. The opportunity for these two movements to become one powerful driving force to truly change the world for the better excites us.

As investors, we have a deep responsibility to our clients to invest for their long-term goals in a sustainable manner. Our approach to sustainable investing has evolved given an increased understanding of how various actions can affect economic growth, the environment, confidence in sound governance practices and financial markets. Sustainably allocating our clients' capital has become a core focus of our portfolio of assets and we believe that this should increasingly become our new standard for investing.

We are excited to announce that we are partnering with Global Steering Group for Impact Investment (GSG) and Impact Investing South Africa (IISA) in hosting the 2020 annual GSG Impact Summit in Johannesburg early September. This will be the first of its kind on the African continent. The Summit assembles leaders and practitioners from across the globe for a two-day conference, where they discuss the current state of Impact Investing and work together to identify global priorities, key action areas and milestones necessary to establish impact investing in the mainstream economy.

The movement is continuing to grow and it's becoming the new way of how we go about our everyday living. As fiduciaries of our clients' assets and having a key role to play in the communities we operate in, we will continue to sharpen our focus in this area and aspire to impact and change the world we live in, in a meaningful way.



2020 ASSET ALLOCATION OUTLOOK

JOHN ORFORD | PORTFOLIO MANAGER

ABOUT THE AUTHOR

As Portfolio Manager, John is responsible for managing the Stable Growth, Moderate Balanced and Real Income unit trusts as well as the Profile Moderate and Profile Capital institutional funds.

KEY TAKEOUTS

- LOOKING AHEAD, WE EXPECT GLOBAL RETURNS TO BE MUCH HARDER TO COME BY IN 2020 AND SEE OPPORTUNITIES IN CHEAPLY PRICED LOCAL ASSETS.
- SOUTH AFRICAN GOVERNMENT BONDS ARE AMONGST THE HIGHEST YIELDING ASSETS AVAILABLE TO GLOBAL INVESTORS AND THIS THEME HAS THE POTENTIAL TO BENEFIT SOUTH AFRICA IN 2020.
- IN REVIEWING OUR LOCAL ASSET CLASS RETURN EXPECTATIONS, WE HAVE FURTHER INCREASED THE EXPECTED LONG-TERM RETURN FROM LOCAL ASSETS.



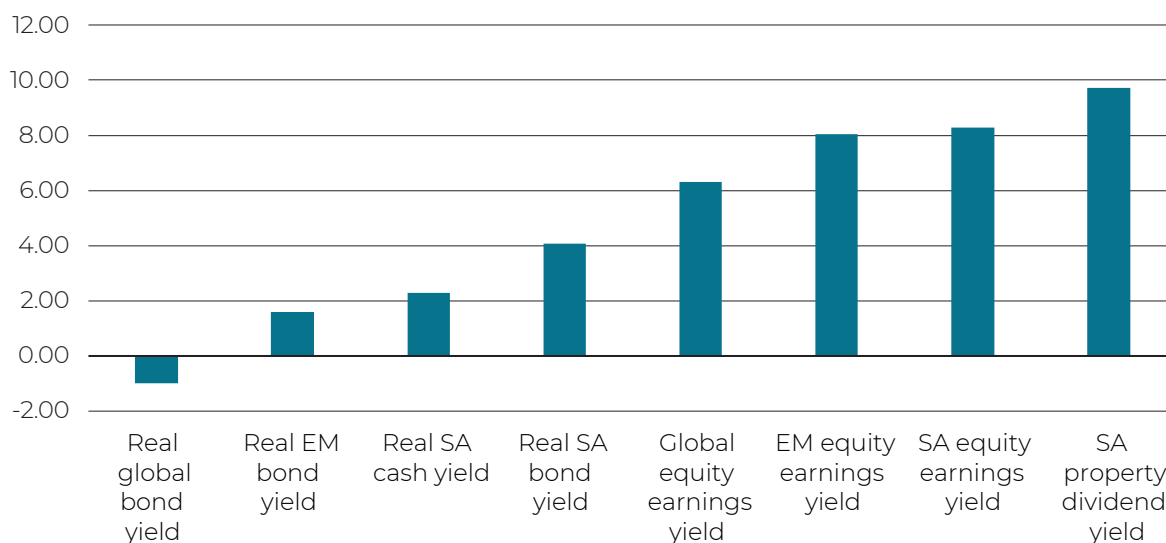


After a rocky 2018, global equity markets have delivered a stellar 24% return in 2019. By contrast, South African equities have had another moderate year with just over 9% return (JSE SWIX) lagging local bond returns in 2019. Looking ahead, we expect global returns to be much harder to come by in 2020 and see opportunities in cheaply priced local assets. Our global view is shaped by the theme that the United States (US) will underperform and we are therefore underweight in US equities within our portfolios. US equities have outperformed global equities for a decade now and valuations are expensive relative to the rest of the world. This outperformance has been supported by a stronger earnings performance from US corporates. We expect the US economy to

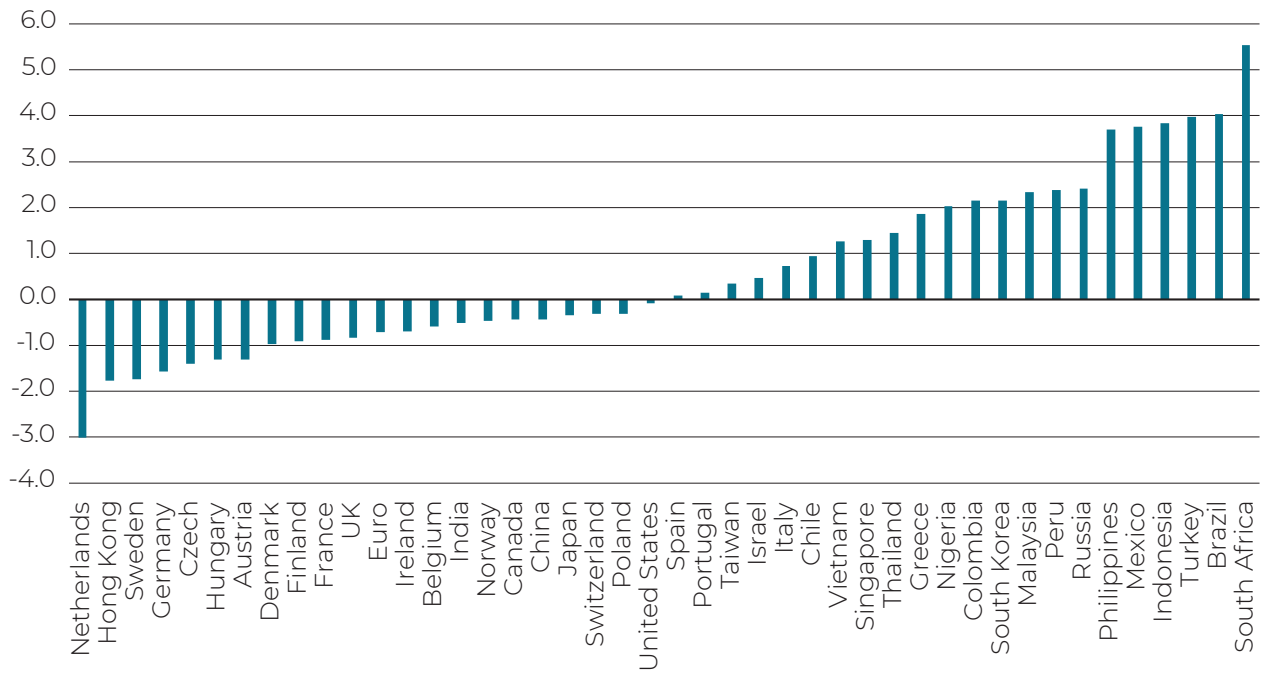
slow down and this is likely to put pressure on US corporate profit margins and earnings.

Another key theme for global markets is the very low yield available in most of the world. About US\$12 trillion worth of global government bonds – a fifth of the total market – trade on negative yields. In other words, investors are prepared to pay the governments issuing these bonds for the privilege of lending them money. We think this will continue to drive capital from areas of low yield to areas of higher yield. South African government bonds are amongst the highest yielding assets available to global investors and this theme has the potential to benefit South Africa in 2020.

WHERE TO GO FOR YIELD



Source: MacroSolutions



Source: MacroSolutions

Of course, to take advantage of these potential capital flows South Africa will need to up the ante on economic reform. We have a theme of “Winds of Change” for South Africa – incremental reforms are gradually resulting in the outlook improving off a low base. It’s clear though that the pace of reform is too slow for the ratings agencies. Both Moody’s and Standard & Poor’s (S&P) have recently downgraded their outlook on South Africa’s sovereign credit ratings from stable to negative implying further downgrades unless progress is made in resolving South Africa’s fiscal crisis and improving growth prospects. Markets, of course, are forward-looking and, while there is likely to be some volatility around a downgrade by Moody’s, the only ratings agency to currently have South Africa rated investment grade, we think local bonds have already priced in much of the bad news. We also see evidence that Government is serious about reform even if it is slow in implementing.

In reviewing our local asset class return expectations we have further increased the expected long-term return from local assets, while reducing the long-term return expected from offshore assets. Our expected

returns for South African assets have generally been revised higher while our expected returns for global equities have been revised lower. On a relative basis, the argument for South African over offshore assets is becoming stronger. South African assets continue to derate – in other words, they are becoming cheaper and offering better value. We have increased our long-term real return expectation for South African equity and property while our return expectation for bonds is unchanged. South African bonds continue to offer exceptional returns when compared to global bonds. We have reduced our return expectations for global equities following the strong rally in global equities. Our return expectations for global cash and bonds remain unchanged and are deeply unattractive.

Combining this into a balanced fund, our expected real return is 4.8% a year for the next five years. This is slightly higher than our previous estimate of 4.6% in July 2019 but much higher than the low point of 3.5% in 2015 when markets were expensive and our main theme was a low return world. The message from our return expectations is that future returns are looking more attractive.

UPDATED RETURN EXPECTATIONS

SA EQUITY

We have increased our expected real (after inflation) return for SA equity by 50 basis points (bps) to 6.5% a year over the next five years, up from 6.0% in July and 5.5% a year ago. The return is driven by a 4.4% dividend yield and a relatively depressed earnings base, which provides a good platform for better growth in the future. However, the improved growth will depend on better growth in the economy.

SA PROPERTY

Our expected real return for property has increased by 50bps to 7.5% per year over the next five years. This is up 50bps on July's estimate and 100bps on a year ago. This is an exceptional return driven by a very high dividend yield. While we remain concerned about the trading environment for property companies, the very high yield means investors cannot ignore property.

SA BONDS

We have maintained our five-year real return expectations for bonds at 4%. South African bonds offer very high real returns compared to global real returns for bonds. In our view, this already prices in further downgrades by credit ratings agencies and our portfolios hold significant positions in government bonds, which we think will deliver excellent risk-adjusted long-term returns.

SA CASH

We have increased our real cash return expectation by 50bps to 2%. One of the implications of an economy that requires foreign capital inflows is that, in the absence of strong growth, real interest rates will need to remain high. While there is some scope for further interest rate cuts this year, inflation is also likely to remain lower and so interest rates look set

to be anchored at relatively high levels. That said, the high real yields on offer in other asset classes mean that investors should remain invested in a diversified portfolio.

GLOBAL EQUITY

The global equity market is becoming increasingly bifurcated between expensive US and growth shares and cheaper rest-of-the-world and value shares. For the long term, given low or negative bond yields, there is no alternative to global equities. However, shorter term we are concerned markets are pricing in a strong profit recovery when, particularly in the US, profits are more likely to fall. We have reduced our five-year real return outlook for global equities to 4.5%* and remain cautiously positioned on the asset class.

GLOBAL BONDS

Nearly US\$12 trillion worth of government bonds – about a fifth of the total market – trade on negative yields. Bond markets are neither bullish on global growth nor expect much by way of inflation. While this forecast may well pan out it leaves very little if anything on the table for investors. Our five-year real return outlook for global bonds remains a very unattractive -1%* per year.

GLOBAL CASH

Global cash is also likely to deliver negative real returns over the next five years and we maintain our outlook for the asset class at -1%*. Central banks have eased policy in response to weaker global growth on the back of the US-China trade war. While the US and China are expected to ease policy further over the next year, there is little that central banks in Europe and Japan can do to bolster growth, given already very easy monetary policy stances. Monetary policy is reaching its limits.



ESG RESEARCH INTEGRATION LESSONS FROM GLENCORE AND STEINHOFF

MERYL PICK | PORTFOLIO MANAGER

ABOUT THE AUTHOR

Meryl is the portfolio manager and the analyst responsible for gold, clothing retail, heavy equipment distributors and logistics companies.

KEY TAKEOUTS

- OUR JOB AS FUND MANAGERS IS NOT TO AVOID RISK ALTOGETHER BUT TO BALANCE RISK APPROPRIATELY WITH POTENTIAL REWARD.
- ESG RESEARCH CASTS A SPOTLIGHT ON UNQUANTIFIABLE RISKS THAT NEED TO BE CONSIDERED WHEN CONSTRUCTING PORTFOLIOS.



Glencore was a significant holding across our funds at the start of 2019, yet over the course of the year we sold the stock to zero. It's not a coincidence that 2019 was also a year in which the investment team drove a step change in how we integrate Environmental, Social and Governance (ESG) research into our investment process. By outlining how we came to our decision on Glencore, I will illustrate how integrating ESG research has enhanced the way we value companies and debate risk.

WHY DID WE BUY GLENCORE?

There are two aspects to our investment process. Firstly, we carry out detailed fundamental bottom-up research. We dedicate a significant amount of time and effort to analyse a company, examining in great depth the business model, the company's key drivers, its future growth prospects, its competitors, its profitability and balance sheet health. The purpose of this work is to determine an estimate of the long-term "intrinsic value" of the business. Our process is based on the philosophy of investing in businesses that trade at a discount to our estimation of "intrinsic value".

However, as Winston Churchill once said, "The future is unknowable, but the past should

give us hope." We acknowledge that there are limitations and biases inherent in our estimates of intrinsic value. Therefore we supplement our bottom-up research with a second aspect that seeks to independently, and in our case quantitatively, "confirm" our fundamental assumptions. The "confirmation" factors assess and score the quality of the company up to that point, its historical and prospective growth and market sentiment towards the share. This ensures that each share is scored and ranked quantitatively by its past independently of analyst input.

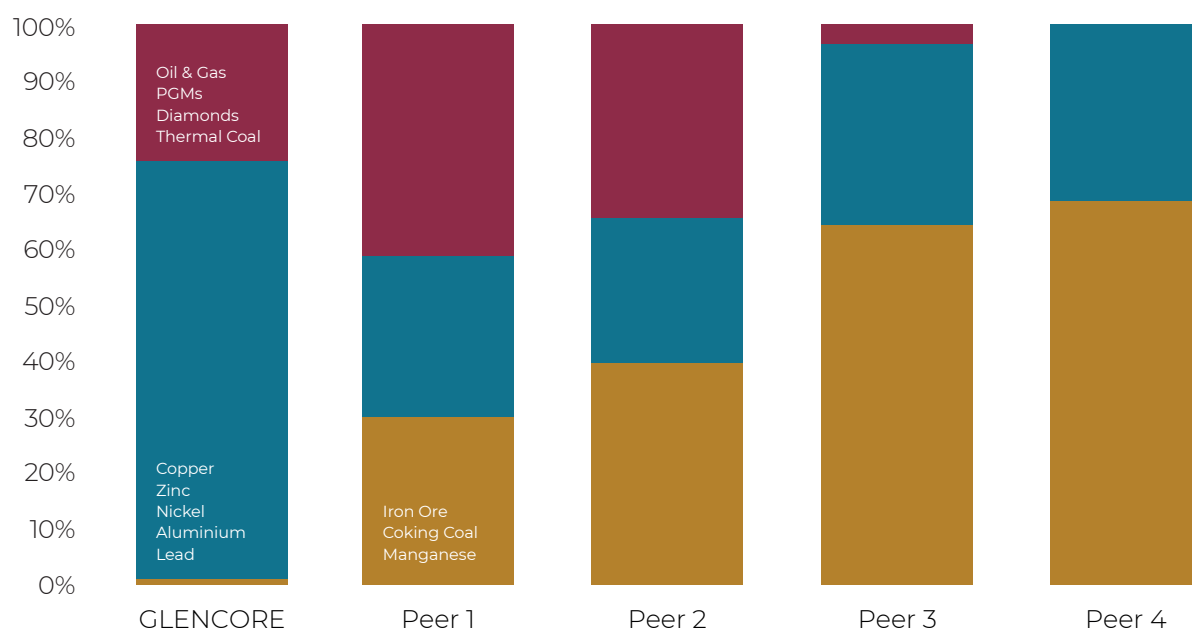
Diversified portfolios are carefully constructed by selecting shares that rank best on both valuation and confirmation factors, while managing overall portfolio volatility. Where valuation meets confirmation, we find our highest conviction ideas.

Our initial investment in Glencore was in 2014. Our fundamental research concluded that Glencore offered significant value relative to the price it was trading at. Glencore is different from the other mining houses listed on the JSE. It has no exposure to iron ore, which in 2014 had risen to levels beyond our estimates of what was sustainable and presented risk of capital loss in investing in other miners.

Glencore has a commodities trading business referred to as the Marketing division – an opaque but a stable and profitable business. Due to the Marketing division's business model, Glencore relies on higher leverage than traditional mining houses. This is a point often misunderstood by the market, which created a further buying opportunity in 2015 when balance sheet fears created panic and overly pessimistic expectations. We continued to invest client funds into Glencore as the price fell to lows of R19 in 2015, and subsequently earned great returns for clients as the price rose to peaks of R68 in 2018. Throughout these years, our quantitatively driven confirmation factors ranked Glencore as a potentially high return investment.

WHAT WAS DIFFERENT THIS TIME?

Glencore had made headlines for crossing the line before. The company was born out of the private holding company of Holocaust refugee turned billionaire Marc Rich, who pioneered the disruption of the spot oil market by displacing the in-house traders of big oil producers in the 1970s. Rich's infamous legacy includes making the FBI's most wanted list. He left the US in the 1980s for Switzerland to avoid charges of tax fraud and trading with



Sources: Glencore investor presentation; UBS estimates of contribution to 2018 EBITDA forecast

sanctioned nations. In 2017, Glencore's dealings in the DRC with Dan Gertler, a controversial Israeli mining magnate, came under scrutiny. Earlier in 2018, the United States Department of Justice announced an investigation into money laundering and corruption focused on Nigeria, the DRC and Venezuela. The Katanga restatement was signalled the year before. So why was this headline troubling?

STEINHOFF CHANGED THE LANDSCAPE FOR DEALING WITH ESG RISKS

The post-Steinhoff era has been characterised by an elevated level of focus on ESG issues from clients and fund managers alike. Over the course of 2018, the

investment team wrestled with this critical question: How did our process miss the Steinhoff risks?

When we invested in Steinhoff, the investment case was aligned with our philosophy and we had followed our process. Our detailed, bottom-up fundamental research concluded that Steinhoff was undervalued and supported a buy. Our conviction in our valuation was supported by our quantitative "confirmation" factors. We saw catalysts on the horizon to unlock that value. Yet our exposure had cost clients in 2017. Even as rumours of accounting irregularities emerged in the German press, we held a position believing that the discount to our valuation was compelling enough to compensate for the governance risks. That belief

was proven incorrect. Were we making a similar mistake with Glencore in assuming the potential rewards justified the potential risks? The key lesson from Steinhoff was that there are times when the biggest risks cannot be adequately quantified.

INTEGRATING ESG RESEARCH INTO THE GLENCORE INVESTMENT CASE

As an investment team we have grappled with integration of ESG issues in our investment and ownership process since 2012. We have built a credible process around proxy voting and engagement on key ESG matters. By contrast, consistently embedding ESG research into our investment process has proven more difficult. It was

once not uncommon for ESG issues, particularly unquantifiable ones, to be treated as a “margin of safety” consideration with more quantifiable valuation work being the primary focus. In 2019, we ratcheted up our ESG integration efforts by revisiting the investment cases of our key holdings while paying specific attention to ESG issues. Glencore was one of the holdings reviewed and several issues were highlighted. I will expand on two of significance: the structural headwinds facing coal and the accounting risk inherent in the Marketing division.

COAL SUBSTITUTION – AN ENVIRONMENTAL ISSUE AFFECTING GLENCORE’S FUTURE CASH FLOW

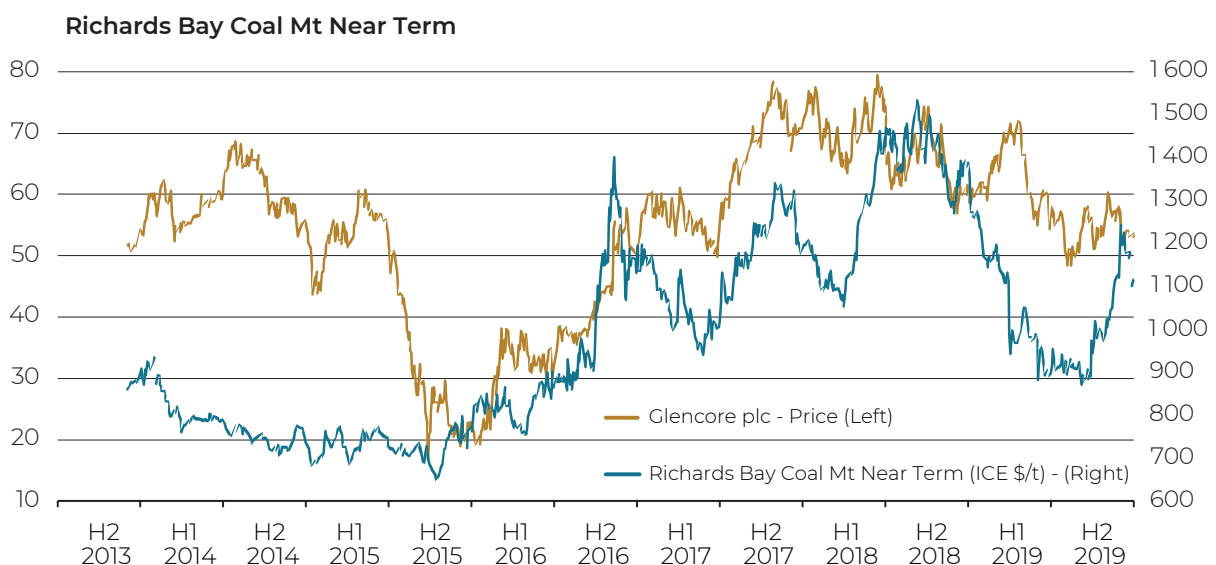
Coal is a substantial part of Glencore’s commodity mix, and the share price often weakens in tandem with coal price weakness. Our ESG analysis emphasised the risk of the uncertainty of coal’s future as a source of energy. As more natural gas fields have been exploited, the price of gas has fallen. Natural gas is a less carbon-intensive source of energy relative to coal. As gas has become cheaper, many countries have pivoted away from thermal coal towards natural gas to meet their energy needs with a smaller carbon footprint. This shift has created a structural ceiling on coal prices. While miners often make up for lower prices with increased volume, Glencore cannot employ that strategy in this case. Climate Action 100+, an investor initiative that ensures

the world’s largest corporate greenhouse gas emitters take necessary action on climate change, includes Glencore on its list as contributing the most. In response to pressure from the activist investor group, Glencore committed to capping its coal production at 2019 levels, thereby limiting further volume growth. This environmental issue is having a tangible impact on future cash flows.

GLENCORE’S MARKETING DIVISION FLAGGED FOR RISK OF ACCOUNTING IRREGULARITIES

Glencore’s Marketing division accounts for 15% to 30% of the group’s EBITDA depending on the profitability of the mining operations. The Marketing

GLENCORE’S SHARE PRICE IS INFLUENCED BY THE COAL PRICE



Source: Factset

division was expanded around the commodities trading business that Marc Rich established in the 1970s. Ivan Glasenberg, company CEO and owner of 9% of listed shares, rose through the ranks in Marketing, as did many of the senior executives. Marketing's business model is to broker sales between commodity producers and customers globally and manage the logistics involved. Revenue is derived from high volumes of transactions across more than 90 commodities, derivatives are widely used and discretion is required to

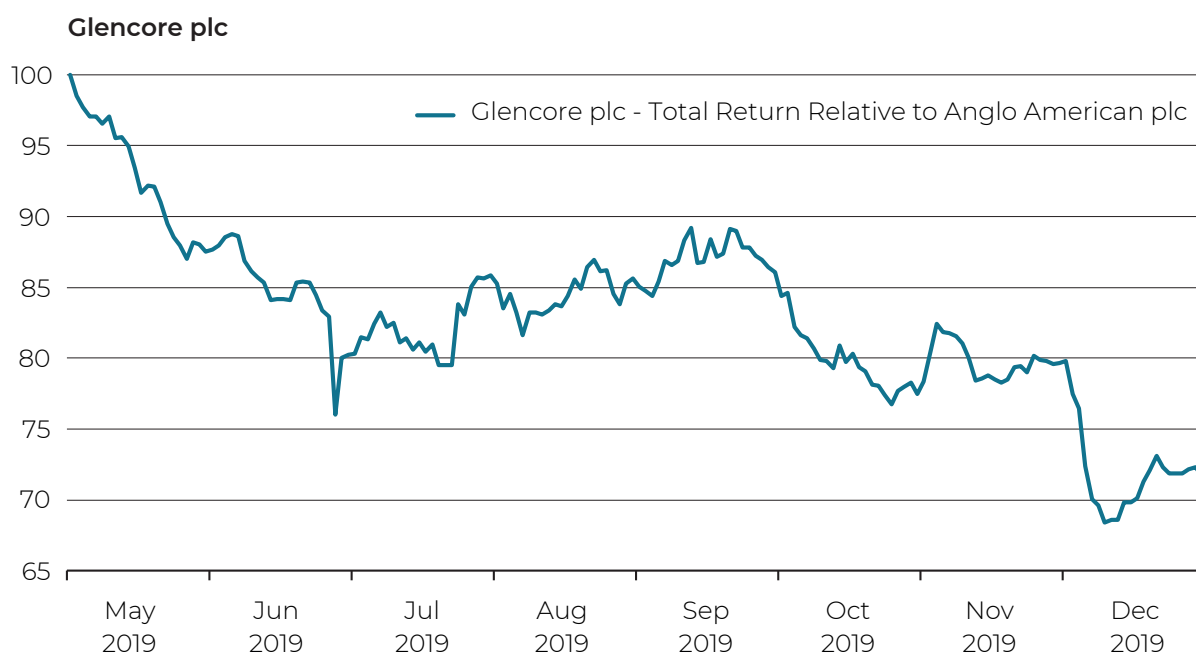
determine when a sale has taken place under long-term contracts held with customers. The nature of these contracts means that the accounting is complex and opaque. Revenue recognition has been flagged as a key audit risk by the auditors over a number of years.

SELLING GLENCORE – NOT EVERYTHING THAT COUNTS CAN BE COUNTED

We took the decision to switch our Glencore shares into Anglo American, which at the time offered value – though less so

than Glencore – with significantly lower risk. We arrived at this decision after weighing up the valuation work, the confirming quality, growth and sentiment factors, the coal price scenarios and the growing list of governance concerns.

Our job as fund managers is not to avoid risk altogether but to balance risk appropriately with potential reward. A coal price in a peak coal world? This can be estimated to inform a judgement call. But when it comes to valuation, how cheap is cheap enough to compensate for poor governance and the risk of accounting irregularities? As





the common quote says, “Not everything that can be counted counts. Not everything that counts can be counted.”

INTEGRATING ESG RESEARCH WILL ENHANCE OUR ABILITY TO DELIVER SUPERIOR RISK-ADJUSTED RETURNS

The goal with integrating ESG research into the investment process is to reach a point where there is no longer “ESG research” and “bottom-up research”, but just research. The encouraging shift is the extent to which ESG issues have been elevated in investment debates. They are blending into conversations with company management alongside topics like competitor

activity and managing working capital. Addressing ESG issues has the potential to become a box-ticking exercise, but we believe that integrating ESG authentically has the power to enhance our process.

Starting with bottom-up analysis, considering the cash flow impacts of ESG issues has sharpened our ability to forecast cash flows, assess companies’ ability to service debt and to pay dividends. ESG research has expanded our vision range in spotting unrealistic market expectations implied in share prices. As with valuation work, ESG research is forward-looking and subjective in nature, hence we believe in confirming our fundamental research by

evaluating stocks on quantitative quality, growth and sentiment factors based on historic data.

Most importantly, ESG research has cast a spotlight on unquantifiable risks that need to be considered when constructing portfolios. We select shares that rank best on both valuation and confirmation factors while managing overall portfolio volatility. Where valuation meets confirmation, we find our highest conviction ideas. However, neither our valuation nor our confirmation factors can always “count everything that counts”. Therefore, integrating ESG research will enhance our ability to deliver superior risk-adjusted investment performance to clients.





A REVIEW OF THE REGULATORY ENVIRONMENT FOR THE GREEN ECONOMY

ROBERT LEWENSON | HEAD OF ESG ENGAGEMENT

ABOUT THE AUTHOR

As Head of ESG Engagement, Robert is responsible for proxy voting and engagement representing OMIG on various industry bodies and championing responsible investment for the group.

KEY TAKEOUTS



- MODERN GROWTH MODELS ALLOW US TO TRACE THE DISCOURSE OF THE GREEN ECONOMY CONCEPT.
- THE GREEN ECONOMY IS INFRASTRUCTURE OR ASSETS THAT BY THEIR NATURE ARE LOW CARBON, RESOURCE EFFICIENT AND SOCIALLY INCLUSIVE.
- LOCALLY, THE MOST IMPORTANT LEGISLATION TO ENABLE INVESTMENT IN THE GREEN ECONOMY IS REGULATION 28 (REG 28) TO THE PENSION FUNDS ACT.

WHAT IS THE GREEN ECONOMY AND WHY SHOULD WE INVEST IN IT?

“The Limits to Growth” report published in *1972 is one of the first publications to raise concerns about the sustainability of modern growth models. Though disregarded and heavily criticised at the time, today the warnings in that report allow us the ability to trace the discourse of the green economy concept.

Today, the United Nations defines the green economy as infrastructure or assets that by their nature are low carbon, resource efficient and/or socially inclusive. In a green economy, growth in employment and income are driven by public and private investment in economic activities, infrastructure

and assets that allow reduced carbon emissions and pollution, enhance energy and resource efficiency, and prevent the loss of biodiversity and ecosystem services.

There are many reasons for investing in the green economy, the most important one being the ability to achieve a reasonable return on investment as mandated by our clients. However, the benefits to our clients are further multiplied by the benefits to society and the environment.

THE GLOBAL AND LOCAL REGULATORY LANDSCAPE

One of the most important global regulatory developments in 2019 for the green economy was the European Union’s creation of the world’s first-ever “green list” – a classification system for sustainable economic activities, or taxonomy. The green list



creates a common language that investors can use everywhere when investing in projects and economic activities that have a substantial positive impact on the climate and the environment. According to the European Commission, it will help scale up private and public investments to finance the transition to a climate-neutral and green economy, redirecting capital to economic activities and projects that are truly sustainable.

Locally, one of the most important pieces of investment legislation

to enable investment in the green economy is Regulation 28 (Reg 28) to the Pension Funds Act. The Pension Funds Act aims to ensure that the savings South Africans contribute towards their retirement are invested in a prudent manner that not only protects the retirement fund member but is also channeled in ways that achieve economic development and growth.

To achieve economic development and growth – key to investment in the green economy – Reg 28 prescribes that a pension

fund must diversify its assets into various asset classes and promote responsible investment. Here we mean considering Environmental, Social and Governance (ESG) factors and acting as a responsible steward of fund assets. These intentions are based on a sustainable, long-term, risk-aligned and liability-driven investment philosophy. This prudent approach to investing considers factors which affect the sustainable performance of a fund's assets, where it then naturally follows that green

economy investments are a responsible way of giving effect to Reg 28.

However, whilst being lauded as one of the first regulations to be enacted globally to prescribe responsible investment, Reg 28 falls short on prescribing to pension funds how to invest that money in the green economy. An important ongoing development is the process underway to develop a taxonomy for the green economy, spearheaded by National Treasury. It is aimed at developing a national strategic framework on sustainable finance and investments cutting across all industries in the financial sector.

In addition, access to investment in the green economy also cuts across asset classes, and regulation has been enacted. For

example, in 2017 the JSE launched a Green Bond segment and aligned its JSE Green Bond listing requirements with international best practice. In the context of the South African economy, it includes specific rules pertaining to green bonds. Issuers of green bonds can raise the capital they need to bring their green economy investments to life, while investors can satisfy critical ESG mandates and address climate risks as a part of their portfolio construction.

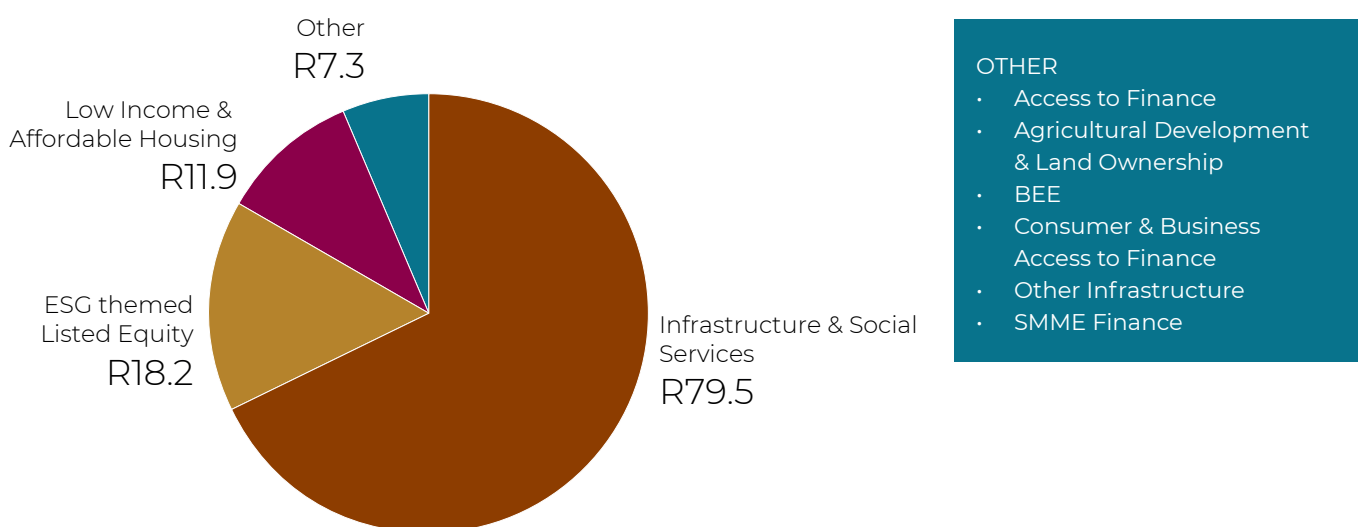
CAPTURING INVESTABLE OPPORTUNITIES IN THE GREEN ECONOMY

As an investment manager, OMIG is primarily a “mandate taker” and not a “mandate maker”. Our commitment to our clients is to manage their assets responsibly,

and in doing so, provide our clients with opportunities in different asset classes to invest directly in the green economy. Whether in listed equity via our ESG indexation funds, fixed income through green bonds or directly in alternative assets in our IDEAS and Development Impact Funds, we’ve taken the opportunity over a few years to take advantage of the upsurge in green economy legislation as well as to influence the development of regulation where necessary. As at 30 June 2019, our total green economy investment value of R117 billion represented approximately 20% of OMIG’s assets under management.

The graph below shows a breakdown of the assets invested by OMIG in the green economy.

ASSET EXPOSURE TO GREEN ECONOMY THEMES - TOTAL AUM (R'BN)





We are confident of the breakdown in assets invested by OMIG into the green economy, as each investment has been tagged using a similar methodology to the European Union (EU). In the absence of local regulation we've developed our own methodology by creating a green list taxonomy to ensure that the underlying investment has a role to play in the green economy. As we invest in global assets, we consider it important to ensure the taxonomy assesses which geographies our green economy

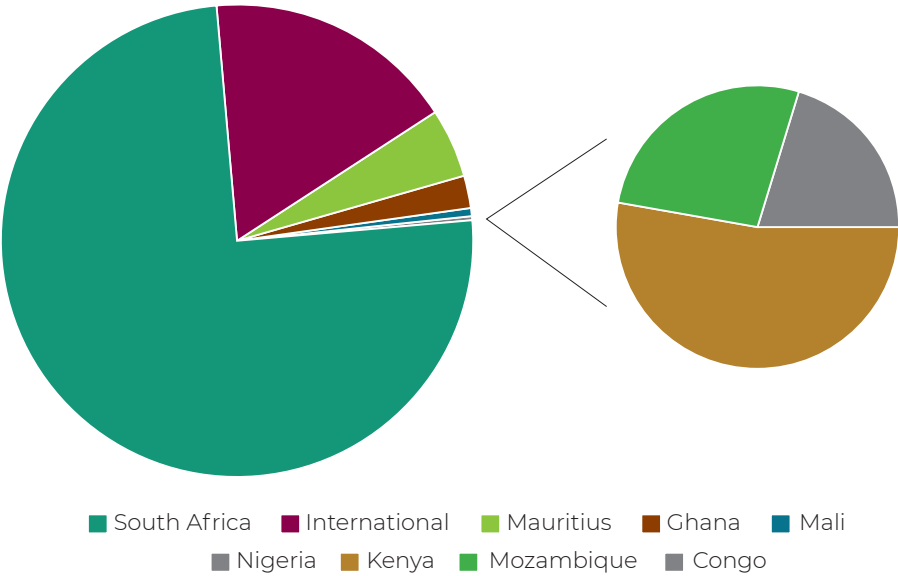
investments are contributing to. This is displayed in Graph 2.

THE FUTURE IS GREEN

Looking at global trends, we see significant growth in the global green economy in the years ahead. OMIG will continue to develop innovative products to offer our clients the best opportunities to access these investments, as well as championing the development of regulation locally and internationally, in supporting a developing green economy.

Later this year, OMIG will be the proud sponsor of the prestigious Global Steering Group (GSG) Impact Summit 2020. This is an annual gathering of impact leaders and practitioners that discuss the current state of impact investing and work together to identify global priorities, key action areas and milestones necessary to make impact investing a mainstream practice.

TOTAL AUM BY COUNTRY



Ground-breaking research, A Legal Framework for Impact, will explore existing legal frameworks to analyse the extent to which asset owners can prioritise sustainability impact, including where this may lead to a negative effect on investment return. In the case of investment managers, it will also explore how they can or should address sustainability impact where their investment mandate is silent on sustainability impact.



CASE STUDY: AN EDUCATION SECTOR GEARED FOR IMPACT

DEAN ALBOROUGH | HEAD OF ESG – OLD MUTUAL
ALTERNATIVE INVESTMENTS (OMAI)

ILSE ZAGER | ESG ADVISOR: IMPACT FUNDS – OLD
MUTUAL ALTERNATIVE INVESTMENTS (OMAI)

ABOUT THE AUTHORS

As the Head of ESG, Dean is responsible for impact investing practice and manages ESG systems and the ESG performance of OMAI's assets.

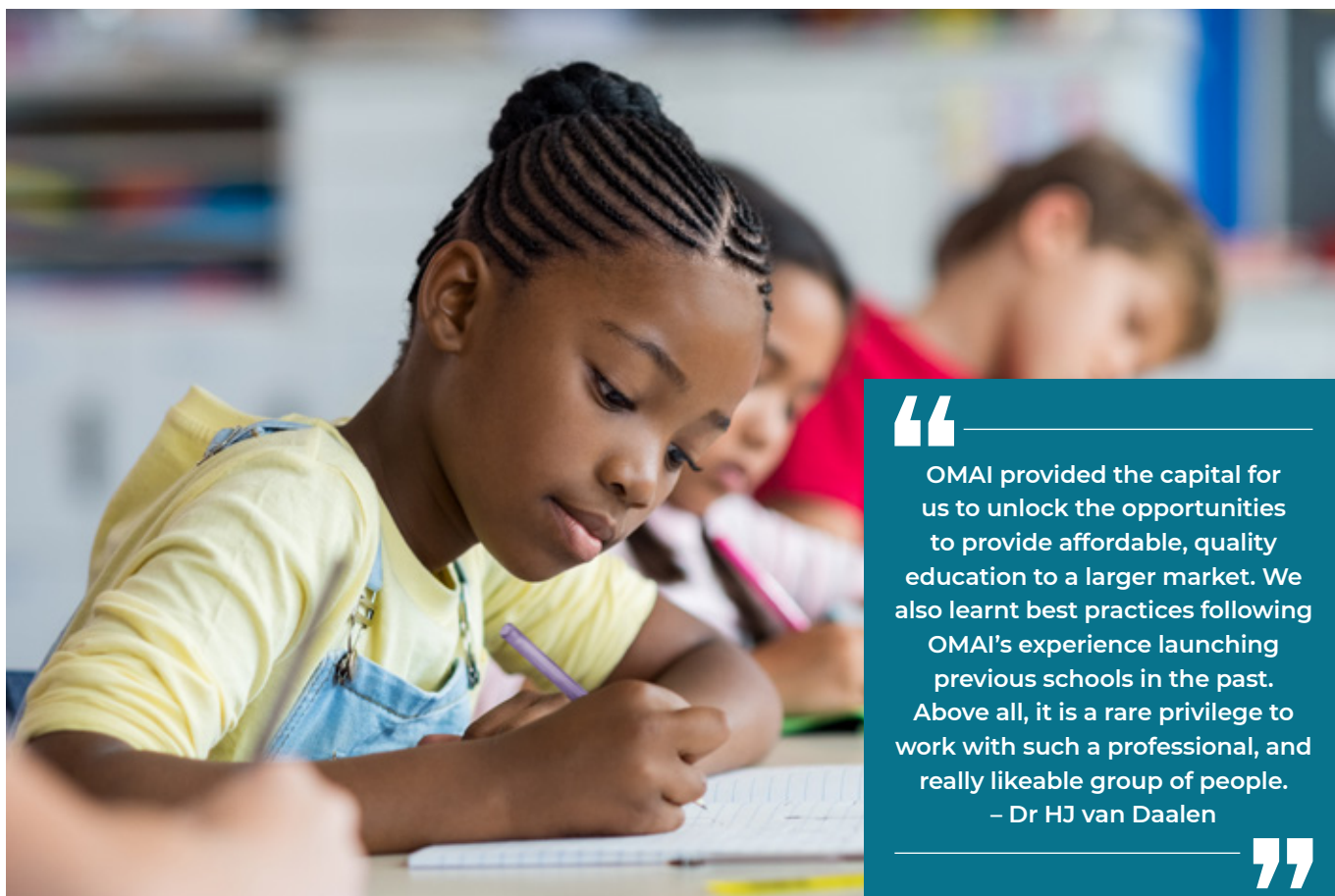
As ESG Advisor, Ilse is responsible for undertaking environmental, social and governance activities across all transactions' execution and asset management for the impact funds.

Impact investing can be viewed as a subset of good ESG practice. The International Finance Corporation (IFC) recently defined impact investing as "investments made in companies or organisations with the intent to contribute measurable positive social or environmental impact, alongside a financial return". It then follows that there are four key elements that an impact investment must embody: intent, a positive impactful contribution, means of measurement and a financial return.

In addressing the challenges in the domestic education sector, Old Mutual Alternative Investments (OMAI) has been investing in the South African education sector since 2011, through the Schools and Education Investment Impact Fund of South Africa (Schools Fund). The primary focus of the Fund is on improving the level of education by creating access to affordable independent schools, while achieving a commercially acceptable return. The first and largest education impact fund in South Africa, the Schools Fund has fully allocated its R1.4bn and further funds are being raised. The Fund had about 21 000

KEY TAKEOUTS

- IN ADDRESSING THE CHALLENGES IN THE SOUTH AFRICAN EDUCATION SECTOR, OMAI HAS BEEN INVESTING IN THE EDUCATION SECTOR SINCE 2011.
- THE PRIMARY FOCUS OF THE SCHOOLS FUND IS ON IMPROVING THE LEVEL OF EDUCATION BY CREATING ACCESS TO AFFORDABLE INDEPENDENT SCHOOLS, WHILE ACHIEVING A COMMERCIALY ACCEPTABLE RETURN.



“ OMAI provided the capital for us to unlock the opportunities to provide affordable, quality education to a larger market. We also learnt best practices following OMAI’s experience launching previous schools in the past. Above all, it is a rare privilege to work with such a professional, and really likeable group of people. – Dr HJ van Daalen ”

learners enrolled in 2019 across 36 schools, with 1 300 staff employed, the majority being teachers. The Fund’s pass rate of 92% in 2019 exceeded the national average of 81.3% and the university exemption rate of 48.1% outperformed the national average of 36.9%. The St Christopher’s School is an example of the positive impact achievable in the broader education sector.

The van Daalen family acquired their first school, St Christopher’s School in King William’s Town, in 2003. Initially with 210 learners, St Christopher’s grew to a fully functional combined school of over 1 000 learners by 2019.

In 2017, with the support of OMAI, construction began on a second school in Kidd’s Beach, outside East London in the Eastern Cape, with the first ten classrooms ready for the January 2018 intake, opening with 171 learners. In its second year, the school exceeded its target of 380 learners to achieve a

growth rate of 140%, breaking the 400-learner mark. The current capacity of the school is 620 learners, which include primary and high school learners. At less than R20 000 per annum school fees (2019), St Christopher’s provides access to quality affordable education to lower- and middle-income families.

Role played by OMAI: The school’s development was made possible by a debt investment of R15m from the Schools Fund managed by OMAI. OMAI maintains a strong relationship with the management team and plays an active role in the investment.

United Nations Sustainable Development Goals (SDG): This investment aligns with UN SDG 4 of Quality Education. OMAI aims to support this goal through its investments in high-quality, affordable schools. The St Christopher’s King William’s Town campus has maintained an average matric pass rate of above 90% for the past 10 years and achieved 98.7% in the 2019 matric results, proving the competence

and quality of the school operator. Similar results are expected for the Kidd’s Beach campus.

THE EDUCATION CHALLENGE IN SOUTH AFRICA

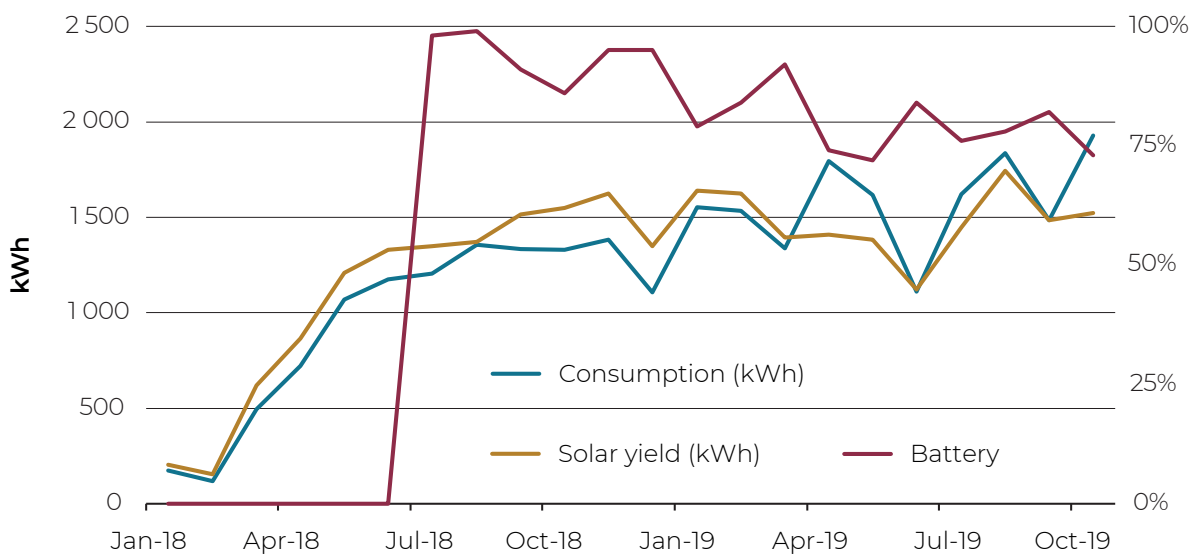
The overburdened public schooling system faces many challenges, including sub-standard infrastructure, poor functionality of governing boards, and limited access to books, teacher absenteeism and an oversupply of vacant posts. The Eastern Cape, for example, had a matric pass rate of 76.5% in 2019. Statistics show that only 51% of Grade 1 learners successfully achieve their matric qualification, while only 48% of learners who were in Grade 10 in 2016 took the matric exam in 2018. South Africa is ranked amongst the lowest performing countries in mathematics, science and literacy. Eight out of ten Grade 4 learners cannot read for meaning. It is within this context that, through investments in quality affordable schools such as St Christopher’s, OMAI aims to contribute to improving the quality of education in the country. Schools in the Fund perform annual numeracy and literacy tests against set targets to continuously improve education outcomes.

TAKING ADVANTAGE OF GREEN ENERGY

OMAI considers many opportunities of positive impact in an investment, and therefore looks at the sustainability of schools from an energy and a water perspective. When the St Christopher’s site was purchased, bulk services needed to be secured. Electricity was a particularly challenging issue, since there was no existing Eskom grid connection available. The management team investigated the installation of a transformer at some R970 000, and along with the inconsistent power supply from Eskom and the reality of continuously increasing cost of power, they decided the best option was to go off-grid.

The current power system consists of 65 x 330W solar rooftop panels with a 57V lithium polymer battery bank, allowing the school to be 100% off the grid with no dependence on Eskom.

SOLAR YIELD VS CONSUMPTION





B-BBEE AND TRANSFORMATION IN A NEW DECADE

TEBOGO NALEDI | DIRECTOR OF INSTITUTIONAL BUSINESS

ABOUT THE AUTHOR

As Director of Institutional Business, Tebogo is responsible for Old Mutual Investment Group's institutional client strategy and execution.

KEY TAKEOUTS

- WE HAVE AN IMPORTANT ROLE TO PLAY IN ADDRESSING THE SYSTEMIC CHALLENGES SA FACES.
- THERE IS A DIRECT CORRELATION BETWEEN THE PROSPERITY OF SOUTH AFRICA AND THAT OF OUR CLIENTS.
- WE BELIEVE TRANSFORMATION IS ALSO ABOUT A CHANGE IN MINDSET AND INTEGRATING AN AUTHENTIC CULTURE INTO THE BUSINESS.



In 2011, Regulation 28 of the Pension Funds Act was amended to, amongst other items, include two guiding investment principles for retirement funds. One of these principles pertained to the Sustainability of Investments (i.e. ESG integration and stewardship) and in June 2019, a guidance note was released by the Financial Sector Conduct Authority (FSCA) outlining the practical considerations that retirement funds should consider with respect to Sustainability of Investments.

The other investment principle pertained to Broad Based Black Economic Empowerment (B-BBEE) and in September 2019, at the inaugural Financial Sector Conduct Authority (FSCA) Retirement Funds conference, the Divisional Executive for Retirement Fund Supervision, Olano Makhubela, announced that in 2020 the FSCA will be issuing a guidance note relating to Broad Based Black Economic Empowerment (B-BBEE) in retirement funds.

This guidance note, like the one on Sustainability Investing issued in June last year, is prepared for principal officers and trustees of retirement funds on how to implement a principle of pension fund legislation, with a focus on section 2c(iii) of Regulation 28 of the Pension Funds Act that states:

“A fund and its board...must at all times in contracting services to the fund or its board, consider the need to promote broad based black economic empowerment of those providing services.” The principle’s objective was to deepen and quicken the pace of transformation in the industry, including asset management companies such as ourselves.

This development follows the inclusion of retirement funds in the B-BBEE Codes and the Financial Sector Charter in 2017 in a voluntary dispensation that supports the requirement “by Regulation 28 of the Pension Funds Act to consider environmental, social and governance (ESG) criteria and B-BBEE as part of their supplier selection processes”. Funds that haven’t done so yet will, therefore, need to engage more

deeply on B-BBEE policy developments and how they should respond in 2020.

As a responsible business and a long-term steward of South Africa’s savings, Old Mutual Investment Group (OMIG) has an important role to play in addressing the systemic challenges of poverty, inequality and unemployment in South Africa. In addressing these challenges, there are critical elements that require focus and attention. These elements are inclusive economic growth, societal transformation and building a sustainable future in which our stakeholders and communities live and operate. There is a direct correlation between the prosperity of South Africa and that of our clients. So, for us, transformation is not just a moral requirement but a business imperative.

OMIG is certified as a **B-BBEE Level 2 contributor**. Although this rating is important, we believe transformation goes beyond ratings and is also about changes in mindset and the true integration of diversity in a business. Our pursuit of investment excellence, and commitment to a future that matters, compel us to drive transformation wherever and whenever we have influence as an enabler of economic activity, a custodian of the nation’s savings, and as a progressive employer.

With that as background, we view transformation for a South African investment management business, like ourselves, as primarily being about four elements:

- 1. Diversity and demographic representation amongst business leaders and investment decision-makers** in the organisation. This is because of the importance of a diverse and inclusive leadership in transforming the organisational psyche to that of authentic inclusivity in the way investment excellence is achieved.
- 2. Black and women shareholding**, which speaks to equitable and inclusive participation in the economics of an industry responsible for managing the country’s savings.

3. Active stewardship with respect to

transformation in investee and portfolio companies. For example, at OMIG our team of ESG specialists actively engage companies we hold in client portfolios on their diversity and inclusion policies and black economic empowerment strategy, with a view to creating a broader impact on the economy with respect to transformation. As an industry, we have a responsibility and an opportunity to ensure that sustainable business practices, of which embracing transformation is critical, are embedded in the assets we invest in on behalf our clients.

4. Targeted investments in assets and portfolios that are aimed at producing transformative outcomes in society, alongside investment return.

For example, portfolios that invest in schools that provide affordable quality education, or portfolios that provide affordable housing for communities. Such investments, whilst providing decent inflation-beating returns for investors, have a very meaningful, measurable and truly broad-based social and transformative impact on our society.

OMIG'S TRANSFORMATION STRATEGY PILLARS



**DIVERSITY AND
DEMOGRAPHIC
REPRESENTATION**



**BLACK AND
WOMEN
SHAREHOLDING**



**ACTIVE STEWARDSHIP
WITH RESPECT TO
TRANSFORMATION**



**IMPACT
PORTFOLIOS**

As OMIG, we take our role and responsibilities in society very seriously when it comes to transformation. We acknowledge that we still have some way to go on a number of the elements discussed above, but we also do celebrate a number of significant strides and targets we have achieved to date.

As retirement funds deal with how to implement the B-BBEE related regulations coming their way, they

must consider transformation and B-BBEE from a holistic point of view given an asset manager's role and responsibilities in society. It is as critical to transform and promote greater inclusion and diversity in our broader economy and in communities, as it is to transform and promote diversity and inclusion internally in our organisations.



MARKET INDICATORS

AS AT 31 DECEMBER 2019

	DY %	P/E Ratio	1 Month %*	12 Months %*
FTSE/JSE All Share Index	3.6	16.3	3.3	12.0
FTSE/JSE Resources Index	4.0	14.1	7.0	28.5
FTSE/JSE Industrial Index	3.4	13.7	2.3	8.9
FTSE/JSE Financial Index	5.6	12.3	0.7	0.6
FTSE/JSE SA Quoted Property Index	9.5	10.5	-2.1	1.9
ALBI BEASSA Bond Index			1.9	10.3
STeFI Money Market Index			0.6	7.3
MSCI World Index (R)			-1.7	24.8
MSCI World Index (\$)			3.0	28.4

* Total return index percentage change.

Economic Indicators		Latest Data	Previous Year
Exchange Rates			
Rand/US\$	December-19	14.00	14.35
Rand/UK Pound	December-19	18.56	18.32
Rand/Euro	December-19	15.69	16.47
Rand/Aus\$	December-19	9.83	10.13
Commodity Prices			
Gold Price (\$)	December-19	1524.5	1280.9
Gold Price (R)	December-19	21393.4	18450.4
Oil Price (\$)	December-19	66.2	54.4
Interest Rates			
Prime Overdraft	December-19	10.0%	10.3%
3-Month NCD Rate	December-19	6.8%	7.1%
R186 Long-bond Yield	December-19	8.3%	8.9%
Inflation			
CPI (y-o-y)	November-19	3.6%	5.2%
Real Economy			
GDP Growth (y-o-y)	September-19	0.2%	0.7%
HCE Growth (y-o-y)	September-19	1.3%	1.4%
Household Consumption Expenditure (HCE) Growth (y-o-y)	September-19	0.8%	0.2%
Gross Fixed Capital Formation (GFCF) Growth (y-o-y)	October-19	-1.1%	2.1%
Manufacturing Production (y-o-y) (seasonally adjusted)			
Balance of Payments			
Trade Balance (cumulative 12-month)	November-19	\$6.1	\$3.3
Current Account (% of GDP)	September-19	-3.7%	-3.7%
Forex Reserves (incl. gold)	November-19	\$804.3	\$697.3

Sources: JSE, Iris, I-Net

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quality education.**

1 300 teachers employed.

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