



INVESTMENT EXCELLENCE THROUGH THE AGES

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Imagine, for a moment, the world as it was in October 1966: Muhammad Ali is the world heavyweight champion. Jack Nicklaus has won the Masters at Augusta. The Beatles' hits are ubiquitous and Star Trek has just been piloted (though South Africa has no TV). The West is led by Lyndon B Johnson, Harold Wilson and Charles De Gaulle. Chairman Mao Zedong is at the helm of China's Communist Party. The US has been at war with Vietnam for eleven years, and in a cold war with the Soviet Union for twenty. Che Guevara is stirring up revolution in Latin America. Two years have passed since Malcolm X's death and civil rights protests rage in the US. Hendrik Verwoerd has been murdered in Parliament. Nelson Mandela is two years into imprisonment on Robben Island. Despite geopolitical tensions and social unrest, innovation and investment continue. Warren Buffett buys 5% of Disney for US\$4 million. The Space Race is in full force. Hewlett

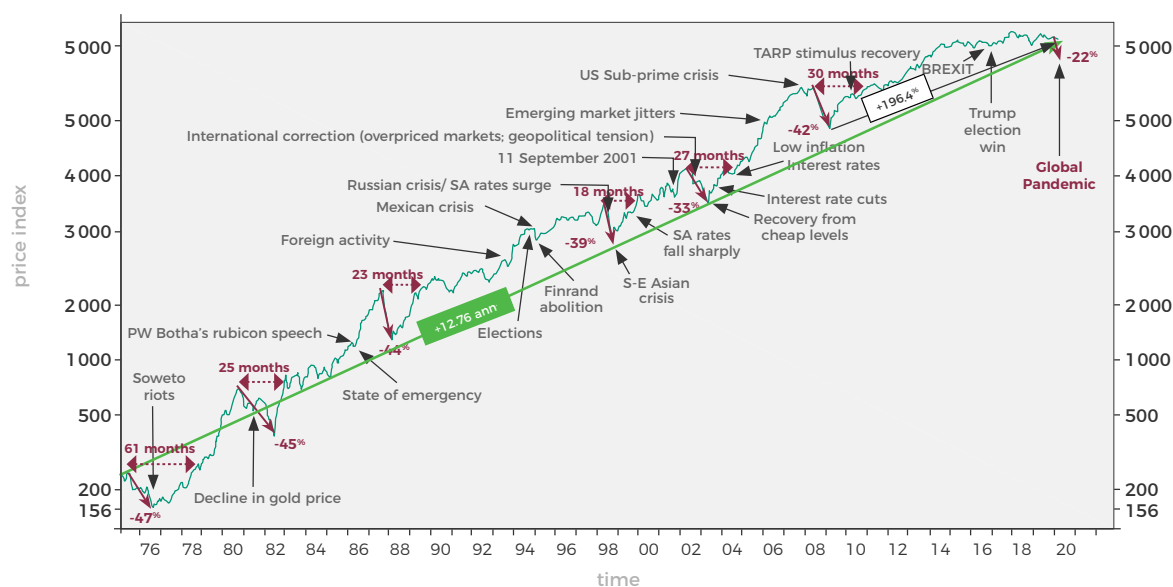
Packard is about to release its first minicomputer. The shoe company Vans is born, the Interbank Card Association (future MasterCard) has just been formed and Old Mutual is launching South Africa's first unit trust.

WE HAVE LEARNT TWO KEY LESSONS FROM NAVIGATING MARKET CRASHES SINCE 1966

The Investors' Fund has grown wealth for clients through nearly 54 years of technological breakthroughs, political turmoil and market booms and busts, delivering an inflation-beating annualised return of 15.6%. Our philosophy is to invest in businesses that trade at attractive valuations. There are two aspects to our investment process. We estimate the long-term "intrinsic value" of a business by examining in great depth the business model, the company's key drivers, its future growth prospects, its competitors, its

profitability and balance sheet health. We supplement our bottom-up research with a second aspect that seeks to independently “confirm” our fundamental assumptions. The “confirmation” factors quantitatively assess and score the quality of the company up to that point, its historical and prospective growth, and market sentiment towards the share. 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. R100 invested in October 1966 would be worth R230 000 today. We reflect on two lessons learnt from navigating several market crashes since then: 1) Catalysts are often unforeseen but cyclical; and 2) Beyond fear lies the opportunity for abundant returns.

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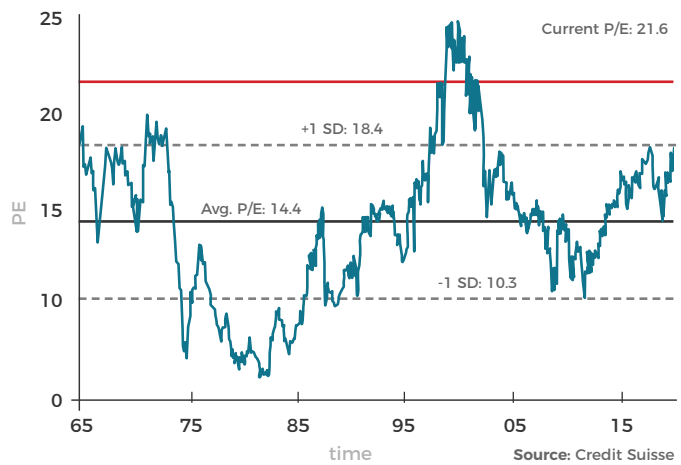
Source: Old Mutual Investment Group, Iress | Updated: 08/06/20 | FTSE/JSE All Share Price Index

Catalysts are often unforeseen but cyclical; and 2) Beyond fear lies the opportunity for abundant returns. On 6 October 1973, Syria and Egypt coordinated surprise military attacks on Israel amidst the observance of Yom Kippur. The US came to Israel's aid by replenishing military supplies, triggering OPEC members to retaliate with an oil embargo. The oil price sky-rocketed and American motorists queued for hours to fill their tanks as panic set in. Against a backdrop of the Vietnam War and Nixon's

Watergate scandal, US inflation climbed into double digits and interest rates followed. Between November 1973 and March 1975, the US was in recession and global GDP slowed. By contrast, South Africa's economy held up well. The countercyclical gold price boosted exports (SA then produced more than 60% of annual gold mined globally) and national defence spending supported GDP. South Africa was relatively independent of oil imports.

In mid-1975 the deepest and longest JSE bear market since the launch of the Investors' Fund set in, with a 47% plunge. As 1975 rolled into 1976, anti-Apartheid protests intensified, conflict with Angola persisted and the easing US recession took the shine off the gold price. Consumer and business confidence fell. During 1976 and 1977, SA suffered its worst recession up to that point since the Second World War. Relief came as stubbornly high global inflation ignited a four-year bull market in gold, starting in September 1976. The economy, and the market, clawed its way back over the next five years.

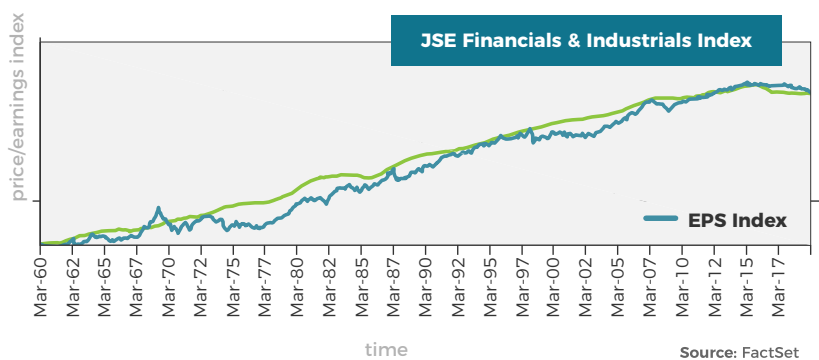
To forecast the catalysts for this cycle, one would have needed to predict a war, a quadrupling of the oil price, wild moves in the gold price, and the Soweto Uprising. However, given that the S&P 500 was trading at a high level relative to history leading up to the 1973 oil crisis, it was a matter of time before falling market returns materialised. Warren Buffett closed his investment partnership in 1969 citing the lack of attractive investment opportunities. Several "Nifty Fifty" shares (high-growth blue chip industrials) were trading at price-earning (P/E) multiples above 50. Similarly, JSE financials and industrials had enjoyed a strong run for three years. At the start of 2020, once again US multiples looked stretched and locally many JSE counters with offshore earnings looked unattractively priced. Since valuation is central to our investment philosophy we had rotated the fund into more attractively priced "SA Inc" shares such as FirstRand, ABSA and Wilson Bayly Holmes. By no means did we forecast a global pandemic, but we had positioned clients' portfolios for a lower return world. Catalysts for market crashes and subsequent recoveries are often unforeseen on the way down and the way up. The only thing that is certain is that cycles are just that, and no condition – not prosperity nor hardship, not bull markets nor bear markets – prevails infinitely.



BEYOND FEAR LIES THE OPPORTUNITY FOR ABUNDANT RETURNS

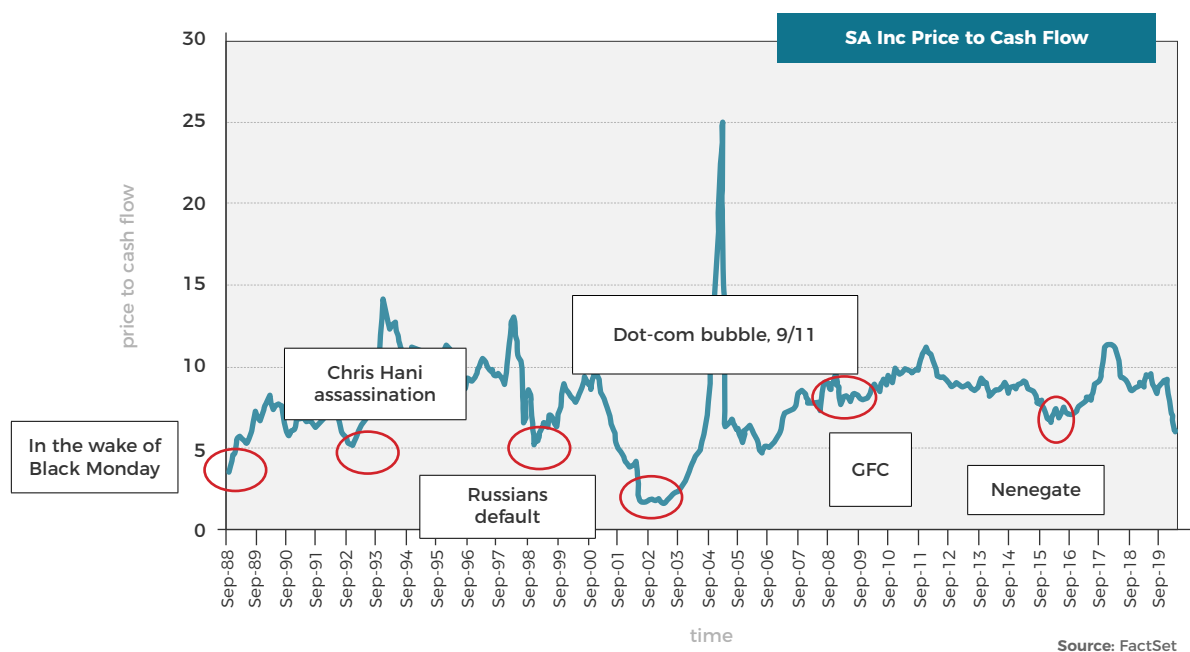
The client who invested in SA equity in September 1976 surely possessed courage and imagination to see beyond the literal and figurative "blood on the streets". Three months earlier, the Soweto Uprising made headlines. Net capital flows into the country were slowing and real GDP growth was approaching zero. However, that investor's decision was rewarded with annualised returns of 44% for the next four years.

The chart below shows the JSE Financials and Industrials earnings index and price index over time. The price index is more volatile than the earnings index, falling to lower lows and rising to higher highs. This illustrates how share price movements are often amplified – positively and negatively - when investor sentiment comes into play. By contrast, earnings are driven by GDP and company strategies. Negative sentiment periodically drives market prices below what is justified by fundamentals and normalized company earnings. What follows from these low lows is a period of strong returns.



Given the cyclical nature of markets, this pattern repeats. From October 1987 to February 1988, the Investors' Fund returned -38% as the US Black Monday Crash triggered a global bear market. Fourteen months later the fund returned 61%. In August 1998, the Investors' Fund fell 37% when Russia defaulted on its debt causing a market crash. Over the next year, returns averaged 36%. Beginning in April 2008, the Investors' Fund declined 27% over a year as the world struggled through the Global Financial Crisis. In the following year, returns averaged 46%. In March of 2020, as the COVID-19 outbreak grew into a global health and economic crisis, the Investors' Fund declined by 20% and returns have averaged -19% over the last

12 months. However, the fund is positioned in line with our philosophy of determining company valuations and seeking conviction through confirmation factors. Many of our "SA Inc" holdings are at valuation levels only reached in previous crises, as illustrated on the Price to Cash Flow chart below. History tells us that a recovery is due. Market crashes often coincide with times of tragedy and uncertainty. It is difficult to maintain a long-term perspective while living through conditions rife with despair and uncertainty. Paradoxically, it is only amidst this pervasive negativity that rare openings for great investments can exist.



WE'VE BEEN HERE BEFORE

The Investors' Fund has navigated several market crashes, with the most recent occurring in March 2020. We did not predict COVID-19 as the catalyst, but believed that the cycle was nearing its peak, particularly in offshore markets and local shares which earn most of their profits offshore. Catalysts are often unforeseen but cyclicity is certain. To prepare for a lower return environment, we positioned the fund in "SA Inc" where company valuations and confirmation factors indicated stronger future returns. As this crisis has unfolded, clients have weathered discomfoting declining returns and many investors may be tempted to withdraw from the market. However, many of our holdings are at valuation levels only reached in previous crises. History tells us that a recovery is due and that beyond fear lies the opportunity for abundant returns.