QC

Quarterly Commentary
Vol. 1 31 March 2022

ALLAN GRAY

Russia–Ukraine conflict accelerates market shifts

CONTENTS

COMMENTS FROM THE CHIEF OPERATING OFFICER

Rob Formby

... it is an opportune time for me to pass the chief operating officer's baton ...

Over the past quarter, the Russia-Ukraine conflict has dominated our minds, eclipsing lingering COVID-19 concerns and increasing the inflationary heat that has been notching up in the face of a strong recovery from demand and supply constraints on the back of the pandemic. Closer to home, the floods in KwaZulu-Natal piled more misery and suffering on a region still recovering from the 2021 riots. In both cases, the human tragedy is immense, and our thoughts are with those who are impacted.

On the investment front, these events reiterate that building well-diversified, resilient portfolios is the best defence against ongoing uncertainty. While major world events tend to have less of an impact over the long term than you would think, the shorter-term direct and indirect consequences can be far-reaching. In the case of the current conflict, oil prices have increased sharply and are close to the highest levels experienced over the past decade. Furthermore, as Russia and Ukraine are global suppliers of agricultural staples, the conflict is likely to lead to an increase in food prices, with few remaining unaffected. There is also heightened market volatility.

Discipline and focus are key

In situations like these, our job as your investment manager is to remain disciplined and focused, assessing the impact on the fundamental value of businesses. We then cautiously invest where we see value and where businesses appear to have the potential to survive and thrive beyond prevailing conditions. This is when it pays off to have an investment philosophy that has been tested through market cycles. Our approach, which we share with our offshore partner, Orbis, enables us to take advantage of whatever types of opportunities the market presents. Alec Cutler, from Orbis, provides insight into how Orbis has been navigating the current investment environment, and discusses the positioning of the Orbis SICAV Global Balanced Fund.

People often ask us to define our investment style/approach, referring to both us and Orbis as "value" managers. But as with many things in life, while labels can help, they sometimes fail to capture the full picture. In his in-depth piece, Grant Pitt explains why we prefer not to be boxed in, and why we rather consider ourselves "value-orientated" investors.

While the theory provides great context, and will help you in understanding why we invest the way we do, we know that the story truly comes to life with examples from our portfolio – and we have two interesting pieces to share with you this quarter: Tim Acker looks at the abrupt reversal of fortunes at Naspers, assessing what has caused its fall from favour and interrogating the investment case, while Siphesihle Zwane discusses the green shoots emerging at Nedbank and explains why they may reward investors who have enough conviction to stay the course.

Regulatory changes aimed at improving your investment outcomes

With headlines dominated by the war, some may have missed an important piece of local news. In the February 2022 Budget speech, the National Treasury announced significant changes to the framework that governs how much of South African retirement savers' portfolios can be invested outside South Africa, opening the door for additional foreign exposure and giving all of us the flexibility to benefit from the offshore opportunity set. While the global news continues to bring much uncertainty, and local investments look attractive, it is best to do some homework before simply diving in. Earl Van Zyl's piece is a great place to start.

> … our job as your investment manager is to remain disciplined and focused, assessing the impact on the fundamental value of businesses.

Another recent change to take note of is the way that tax is calculated for living annuitants. If you are in this group, Carrie Norden's article will help you understand the rationale behind this change and the impact it may have on your take-home living annuity income.

Of course, with any changes, we can reflect on how they would be broadly applicable, but if you need advice for your personal circumstances, it is crucial to talk to a good, independent financial adviser. Thandi Skade makes reference to this in this quarter's Investing Tutorial, which looks at several rules of thumb that are used in investment decision-making and how applicable they are to individual circumstances.

Changing of the guard

After 13 years in the business, and four in my current position, it is an opportune time for me to pass the chief operating officer's baton to Mahesh Cooper. He will assume the role on 3 May 2022, followed by a handover period of at least three months.

Mahesh is no stranger to the business, and indeed many of you may know him well. He was employed at Allan Gray between 2003 and 2017, serving as an executive director from 2006 to 2017 and heading up the Institutional Clients team for over a decade. More recently, in 2020, he was reappointed to Allan Gray's board as a non-executive director. Mahesh has over 20 years of experience in financial services in both corporate and fintech companies, is highly respected by peers and industry colleagues and brings a wealth of knowledge of the SA market.

It has been a privilege to be at the helm of the business, despite the unusual conditions we have faced over the pandemic. Going forward, between Mahesh and Duncan Artus and their capable and passionate teams, you are in very strong hands.

I would also like to take this opportunity to thank you for your trust and support.

Kind regards

Rob Formby

WHAT HAS GONE WRONG WITH NASPERS?

Tim Acker

... the massive size of the discount creates some margin of safety and the potential to unlock significant value in various ways.

For many years, Naspers was the star performer of the South African stock market. The onset of COVID-19 drove the Naspers and Tencent share prices to new heights, as was the case with other technology stocks that benefited from lockdowns. In the last year, this success story has seen an abrupt reversal. Tim Acker investigates what has driven this turn of events and assesses the investment case.

After an extended period of stellar performance, as at 31 March 2022, the Naspers share price was down 51% from its peak in early 2021. The share has now underperformed the market, as represented by the Capped SWIX, over five years, as shown in **Graph 1**. Has something fundamental gone wrong at Naspers, or is there value to be had at the current price?

The Naspers business has evolved many times over the company's 107-year history, from publishing and printing, to pay-TV, to internet holding company. Naspers's purchase of a stake in a tiny Chinese technology company called Tencent in 2001 has created immense value for South African investors, as has the decision to hold the investment for more than 20 years. The success of the Tencent investment has been so extraordinary that it has overshadowed all other parts of the business. In recent years, Naspers's investment portfolio has been split roughly 80% Tencent and 20% everything else. Prosus is a subsidiary company listed in the Netherlands, but shares the underlying investments, so for most purposes, one can think of Naspers and Prosus as the same thing.

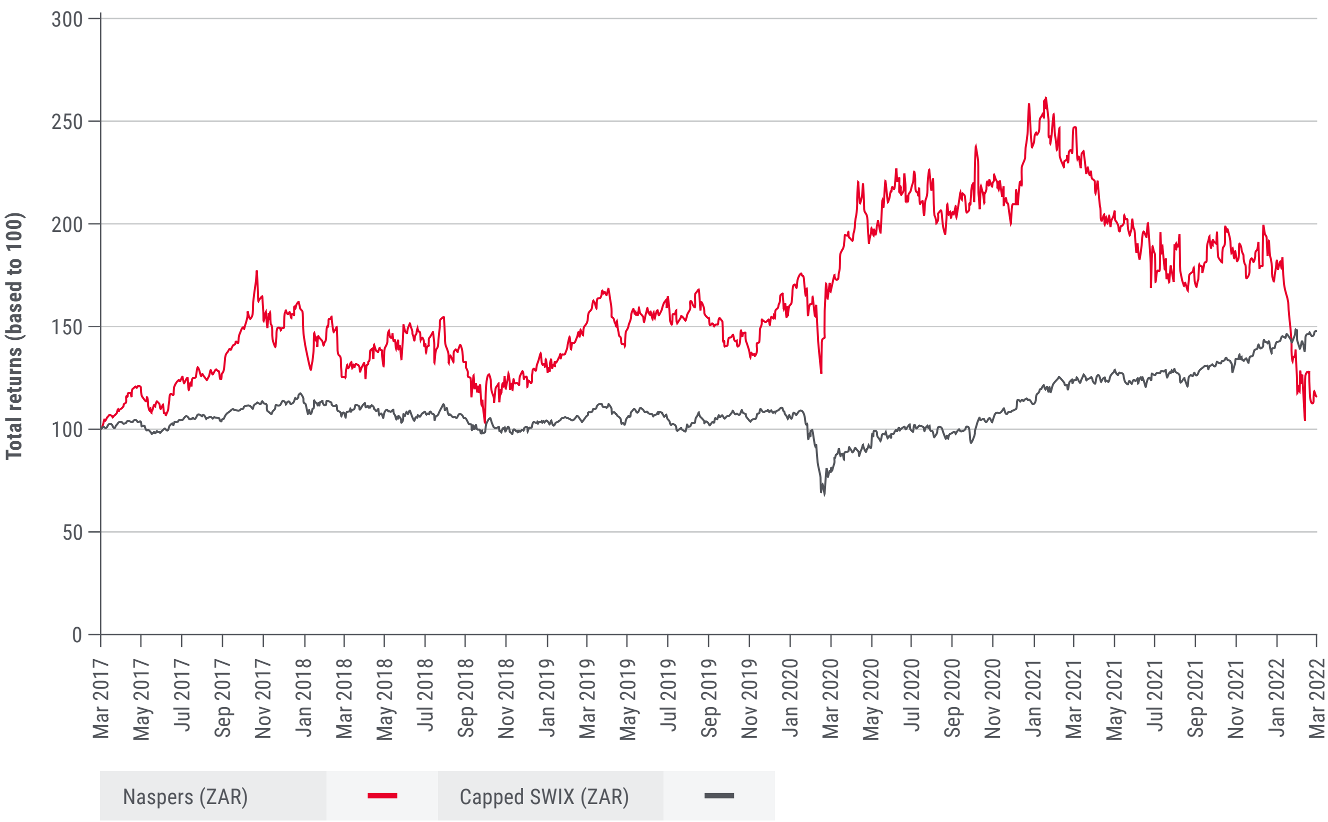
To understand the Naspers business today, what has gone wrong recently, and any future potential, one must look at the business in three parts:

- Tencent
- The collection of other businesses
- The combined value relative to the share price

Tencent

The Tencent share price has taken a beating recently. There are many contributing factors: declining valuations for tech businesses globally, increasing regulatory headwinds in China, a slowing Chinese economy, US rules

Graph 1: Naspers vs. Capped SWIX



Data was adjusted for corporate actions.
Sources: Refinitiv, data to 31.03.2022, company reports, Allan Gray

that may disallow Chinese companies from listing in the US, and a concern that some version of sanctions may be imposed against ownership of Chinese assets (similar to what has recently happened to Russian stocks). In summary, our view is that the intrinsic value of Tencent's business has decreased and the risks have increased.

Our research of regulations imposed by China suggests that some of the negative headlines are noise and will have only a marginal impact on Tencent. Indeed, many of the regulations are catching up to similar regulatory trends in Europe and the US and are not necessarily negative in the long term. However, this is not true in all cases. Some new regulations seem to be intended to transfer value from platform internet companies like Tencent to consumers and small businesses, or seem driven by non-economic objectives of the Chinese government that seem irrational to most Western observers[1]. Some of these variables are inherently hard to predict, such as the Chinese government's next regulatory action, or whether China will align itself more closely to Russia's war in Ukraine, leading to sanctions from the West. These harder-to-predict issues argue for risk mitigation actions, such as a smaller position size in the portfolio.

… our view of intrinsic value has declined, but is still above the price at which the share is trading.

But it is not all bad news. In many ways, Tencent is less at risk than other Chinese tech companies. The business creates value for consumers, advertisers and small and medium-sized enterprises (SMEs), manages regulatory issues well in general and faces little direct risk from the

[1] Two examples are strict rules about the allowable content in new video games, and legally limiting under-18s to only three hours of video games per week.

change in US listing rules (as the primary listing is in Hong Kong). Despite outperforming other Chinese tech stocks, as shown in **Graph 2**, the Tencent share price is still down substantially.

Overall, Tencent's business is still very well positioned in China, with many potential avenues for growth. The valuation is close to the lowest it has been since Tencent listed in 2004. However, it is important to emphasise that the risks have increased, and the possibility of irrational or negative government actions cannot be ruled out.

Other businesses

Naspers started investing in internet businesses in the 1990s. In the early 2000s, following the dotcom crash, it paused for a few years, later resuming investments and then stepping up the pace when the current chief executive officer took over in 2014. Since 2014, Naspers has invested in excess of US$20bn, but has also realised some value from successes such as Flipkart (Indian e-commerce company) and from trimming its stake in Tencent.

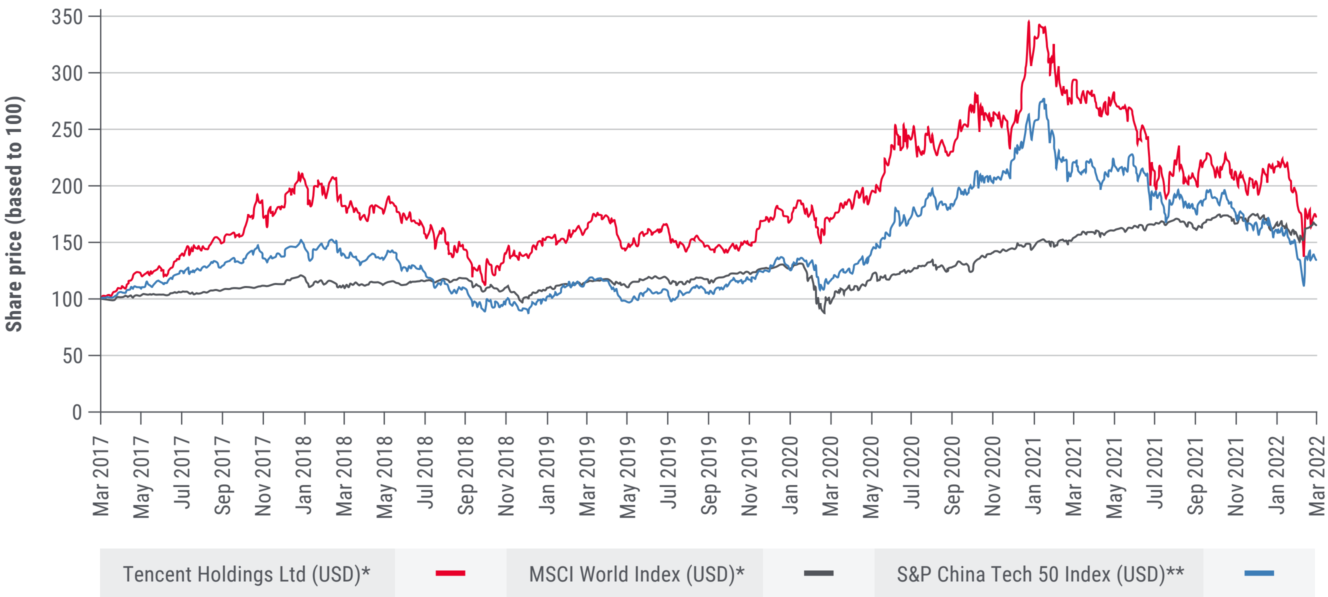
Some of the investments are starting to reach maturity, e.g. OLX (online classifieds business), but many are still in very early stages, such as the various education technology businesses. Naspers has also placed big bets on online food delivery businesses such as Delivery Hero and iFood. These are growing rapidly and offer a large potential prize, but the jury is still out as to whether they can be sustainably profitable. Other investments include the payments company PayU and online retailers eMAG and Takealot. The pay-TV business was distributed to shareholders in 2019.

The investments in these other internet businesses have been funded by dividends from Tencent, which is something investors have often criticised. As with any company, our approach is to look at the underlying businesses and investment decisions in detail, both to form a view of the intrinsic value of these businesses and to assess whether management has been allocating capital well on behalf of shareholders.

In Naspers's case, this is complicated by many of these businesses being at an early stage, resembling a venture capital portfolio, which will have some failures and some large successes. Time will tell whether the investment track record of Naspers's current management team has been good, but so far, the results, excluding Tencent, look unexceptional. Our assessment of the value of these businesses is updated as new data emerges, but is currently lower than management's assessment. Even so, the value is significant at an estimated US$25bn to US$40bn.

Market valuations of unprofitable, early-stage technology businesses have declined significantly over the last year. While this was an overdue correction, in our view, it does unfortunately lower the value at which Naspers can sell

Graph 2: Tencent vs. World Index and China tech



Sources: *Refinitiv, data to 31.03.2022 **Bloomberg, data to 31.03.2022 investments. There are also some positive consequences to lower valuations, such as allowing Naspers to invest new money at lower prices and potentially thinning out the field of competitors for some of its businesses, as capital will be harder to raise.

Combined value relative to the share price

There are many reasons why holding companies trade at discounts to their underlying assets. Discounts of 20% to 30% are fairly common, but very large discounts are often an indication that something has gone wrong, e.g. a loss of confidence in management, poor capital allocation or high running costs.

The Naspers holding company discount has been on a steadily increasing path, with big-step changes when the Prosus structure was introduced in 2019, and again in 2021, when the share exchange and cross-holding were introduced. Both of these were increases in complexity, which the market did not like. Allan Gray recommended a vote against the share exchange transaction. The current structure, while overly complex, does have some advantages, e.g. it is efficient from a tax point of view, and there is potential for simplification down the line.

Much of the public criticism against management for not pursuing a simple structure is valid, but one should also acknowledge that there are obstacles such as regulatory approvals, tax considerations and operational requirements. As shown in **Table 1**, the current discount is very large at 64%; Naspers trades at less than half the value of its underlying investments (see **Graph 3**).

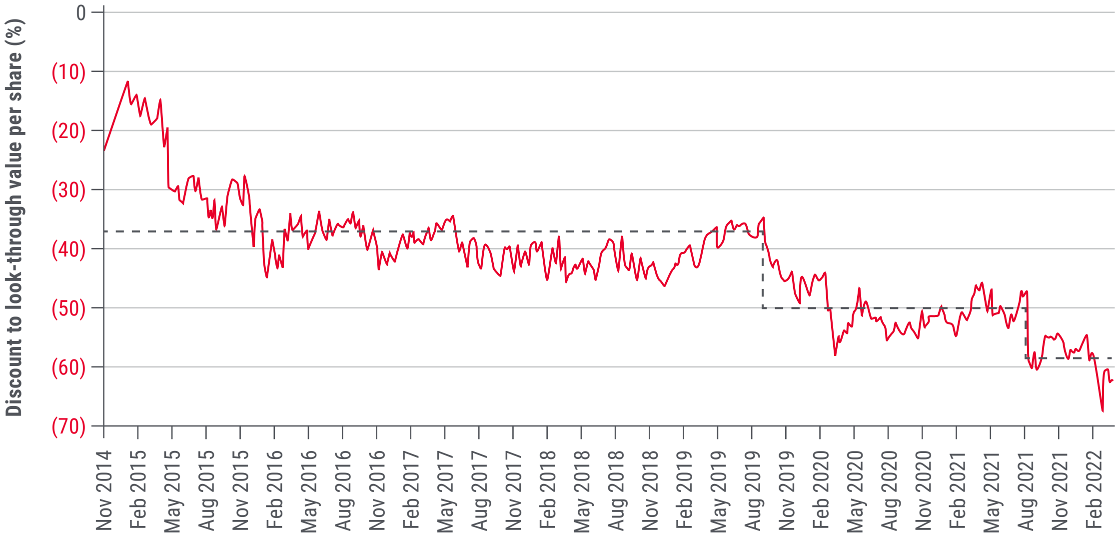
Unfortunately, with Naspers, the trend has been an increasing holding company discount, which has caused the Naspers share price to underperform Tencent. Frustratingly

Table 1: Holding company discount

Asset	Valuation method	Rand per Naspers share
Tencent	Market price	3 760
Other businesses	Latest management valuation less 30%	850
		4 610
Naspers share price		1 664
Discount		-64%

Sources: IRESS, Allan Gray calculations

Graph 3: Discount to value per share



Sources: IRESS, Allan Gray calculations for investors, it is uncertain when and how the Naspers discount will narrow. But the massive size of the discount creates some margin of safety and the potential to unlock significant value in various ways. For example, any asset that Naspers can distribute (or sell and distribute the proceeds) creates an approximately 3x uplift in value (going from 64% discount to no discount on distribution to shareholders). Similarly, buying back shares is highly accretive. At a 64% discount, R1 of asset value can be bought for 36 c – an almost 3x immediate return on any capital deployed. Both these examples are before assuming any narrowing of the discount itself, which would be additional upside.

Currently, we think Naspers/Prosus presents an attractive opportunity, and it makes sense to own a fairly large position.

Naspers management is coming under increasing pressure to unlock value from the structure, rather than pursue new investments. There are different ways in which the structure can be simplified, each with its own trade-offs, for example selling or partially unbundling Tencent, separately listing all the other businesses, or selling off assets individually. Allan Gray recommended a vote against the remuneration policy at the most recent AGM, but there have at least been some improvements to management incentives in recent years, which will hopefully improve alignment with shareholders.

So what has gone wrong?

To come back to answering the title of this article: The share price decline has been caused by several factors. Some have been external factors outside management's control (e.g. a general reduction in valuations of tech companies, a loss of value of Naspers's Russian assets and a sharp turn in sentiment to Chinese assets), and some have been self-inflicted actions (e.g. not unlocking more value from asset sales or unbundlings and overcomplicating the structure). It is too early to make a final judgement about some aspects, e.g. management's investment track record. Regardless of the reasons, some of these factors are likely to be permanent changes that reduce our estimate of the value of Naspers and Prosus shares, while some may be temporary in nature, creating opportunities for long-term investors.

Even though we are value-orientated investors, who buy shares when we believe they are below our estimate of their intrinsic value, a price decline is not automatically a buying signal. We first review our estimate of intrinsic value, considering new information and the various scenarios that could play out. In this case, our view of intrinsic value has declined, but is still above the price at which the share is trading.

Currently, we think Naspers/Prosus presents an attractive opportunity, and it makes sense to own a fairly large position. As always, this may change if our view of the facts changes, or if there are more attractive alternatives. Very importantly, we carefully consider the risk of loss, which plays into factors like the size of the position. Risk is also considered at a portfolio level, e.g. a portfolio's total exposure to China. This last point is important given that many of the large JSE-listed businesses have significant direct or indirect exposure to China.

Tim joined Allan Gray as an equity analyst in 2013 after working in academia and completing his articles. He was appointed as a portfolio manager in 2020 and manages a portion of the equity, balanced and stable portfolios. Tim holds a Master of Accounting degree, specialising in Taxation, from Stellenbosch University. He is a qualified Chartered Accountant and a CFA® charterholder.

BANKING ON GREEN SHOOTS AT NEDBANK

Siphesihle Zwane

… the increasing efficiency of Nedbank's retail business will likely be a driver of value.

The recent pandemic threw the South African banking sector a curveball, causing prices to tumble and creating new opportunities for patient, long-term investors. Siphesihle Zwane discusses the green shoots emerging at Nedbank and explains why they may reward investors who have enough conviction to stay the course.

Banks have a highly geared business model, taking in clients' deposits and lending them out with little equity relative to the size of the lending. Periods of economic stress bring the quality of lending to the fore, and present opportunities to apply our long-term-orientated, valuation-focused process to invest in banks at a discount to our assessment of fair value.

Nedbank is the largest funder in the local commercial property market, funding the purchase and development of malls, offices and warehouses. The pandemic triggered lockdown restrictions on trading and a shift towards a greater number of employees working from home. These developments have deeply impacted Nedbank's clients, creating the perception of heightened risk compared to the rest of the banking industry.

While the risks to Nedbank's balance sheet have increased over the last two years, we believe the business should be able to handle them, in most scenarios, with improving results from its retail bank providing additional upside.

Assessing commercial property balance sheet risks

When assessing balance sheet risks of commercial property lending, we consider the risk of non-payment, the quality of the assets backing the lending, and what larger-than-normal credit losses would mean for the overall business. In the case of Nedbank, the following risks remain well covered:

- **Liquidity constraints:** While the sharp restrictions in 2020 could have created a liquidity crunch, swift reaction from the South African Reserve Bank (SARB) in the form of lowering the benchmark interest rate by 300 basis points and loosening capital and liquidity requirements gave banks and businesses the ability to better handle lower cash flows. At peak restrictions, collections from tenants fell to 67% in April 2020, with listed property funds' pre-interest earnings able to cover 2x the interest due.

- **Asset losses:** The portfolio's loan-to-value ratio is 53%, which means the assets can lose more than half of their value before the bank makes a loss on collateral at a portfolio level.

- **Capital requirements:** Post-global financial crisis (GFC) regulations have meant banks hold more capital. This capital acts as a cushion against balance sheet shocks. At current levels, credit impairments as a percentage of lending would have to be more than 1.8x the COVID-19 peak and almost 2x the GFC highs for the business to wipe out all capital in excess of the SARB's minimum requirements.

The overall property market

The overall property financing market is large, with Nedbank carrying a greater share of the commercial space, and a lower share of the overall market including home loans, as seen in **Graph 1**. It is not obvious that commercial property is riskier than residential property, with the latter experiencing higher economic sensitivity.

Currently, Nedbank's average home loan balance is 79% of property values, compared to 53% in commercial financing. The typical new home loan is currently made at more than 90% loan-to-value, meaning that clients contribute less than R10 for every R100 of the home's value.

Annual expected losses from lending (defaults) are deducted from earnings in the form of credit impairments. **Graph 2** shows the cost of defaults, expressed as a percentage of the overall lending book. The high degree of asset protection has meant that the cost of risk in Nedbank's commercial lending has been less than 0.6% of the book over the last 15 years, with home loans having a more extreme experience over both the GFC and COVID-19 lockdown periods. Commercial property tends to lag the economy given the contractual nature of leases, giving both landlords and lenders more time to prepare for possible losses.

> As valuation-focused investors, we look for companies where market expectations mirror recent trends despite evidence of green shoots.

The retail franchise

While the quality of the lending is important, the best banks have competitive retail franchises that maximise the efficiency of lending, especially in a macro-constrained lending environment. **Graph 3** shows Nedbank's efficiency of lending, measured by non-interest revenue (NIR) after costs per rand of lending. This had been on a sharp negative to 2016, but was improving until the start of COVID-19, as the business focused on efficiency. The bank managed to remove more costs than any associated revenue impact through investing in improved IT systems, with annualised

Graph 1: Commercial vs. overall property market share

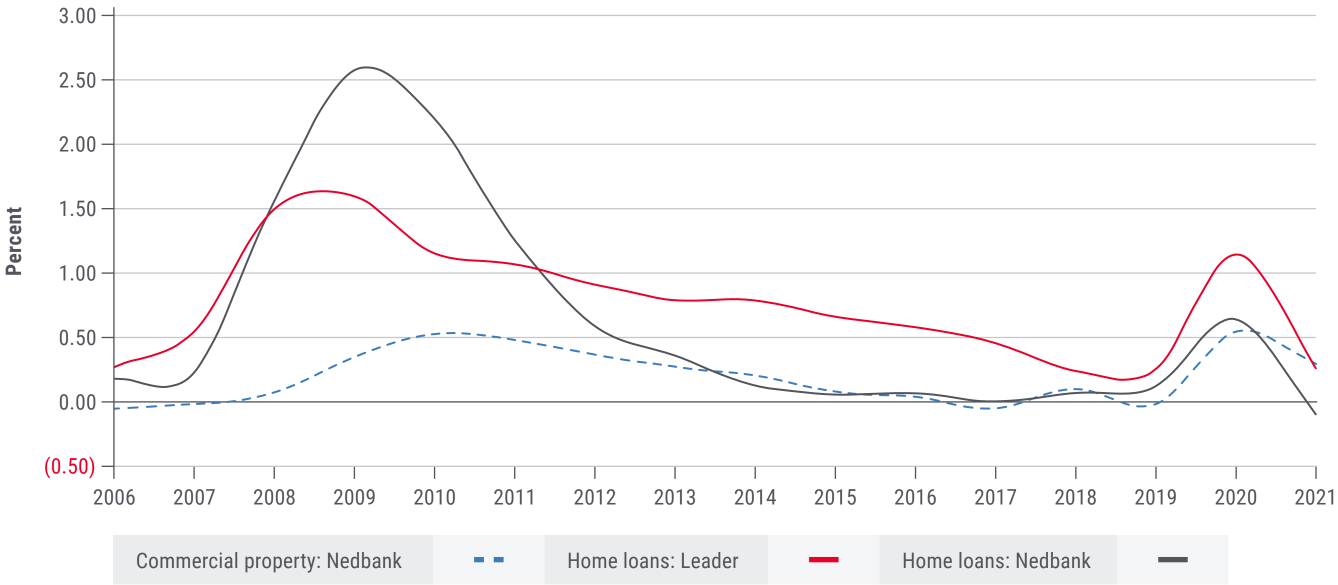
Sources: Company reports, Allan Gray research

IT project costs of R1.7bn compared to R3bn saved. This is in the context where the average fee rate per transaction in the South African banking industry is declining as online fees are often a fraction of what was charged in-branch, forcing cost-cutting to maintain transactional earnings.

Since 2015, Nedbank has reduced office space by 116 000 m², and overall branch space by 45 000 m² by closing a quarter of its branches. This has been achieved while maintaining the industry level of 85% of the target market having access to a branch within 30 km of where they live. Space reductions have been enabled by an increase in the digitally active client base from less than half in 2018 to 64%, which halved teller activity and the related cost base. Increasing digital connectivity allows the bank to provide wider services per client, which offsets some of the per-service fee pressure.

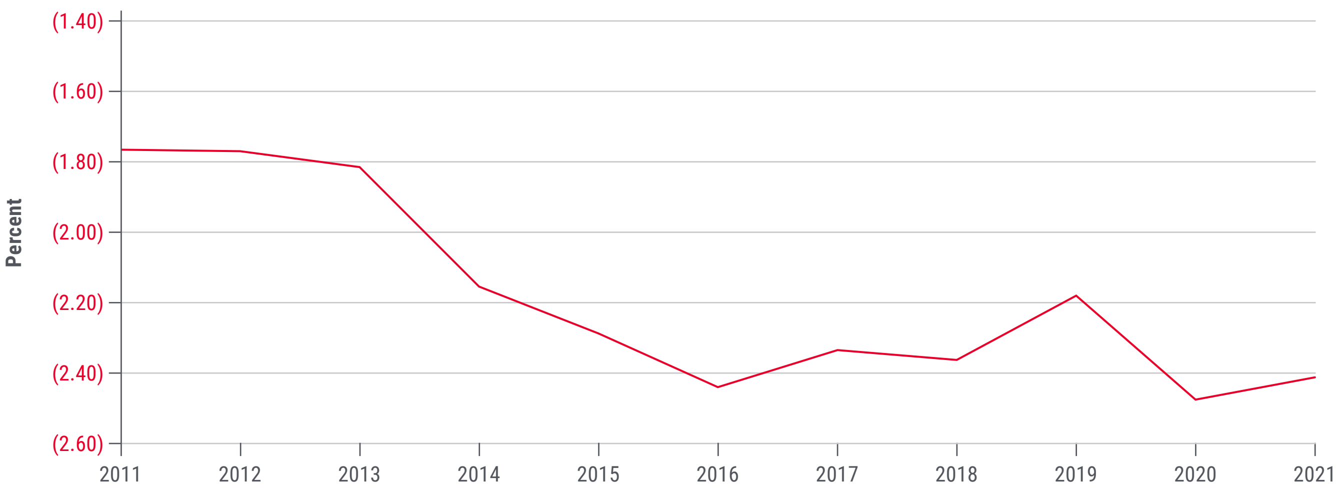
Doing well in an increasingly competitive retail banking environment requires efficient, easy-to-use technology. We think the market underestimates the benefit of the business's steady investments in this area, but on the

Graph 2: Credit loss ratios



Source: Company reports

Graph 3: Retail bank efficiency*



*Measured by non-interest revenue (NIR) after costs per rand of lending.
Sources: Company reports, Allan Gray research

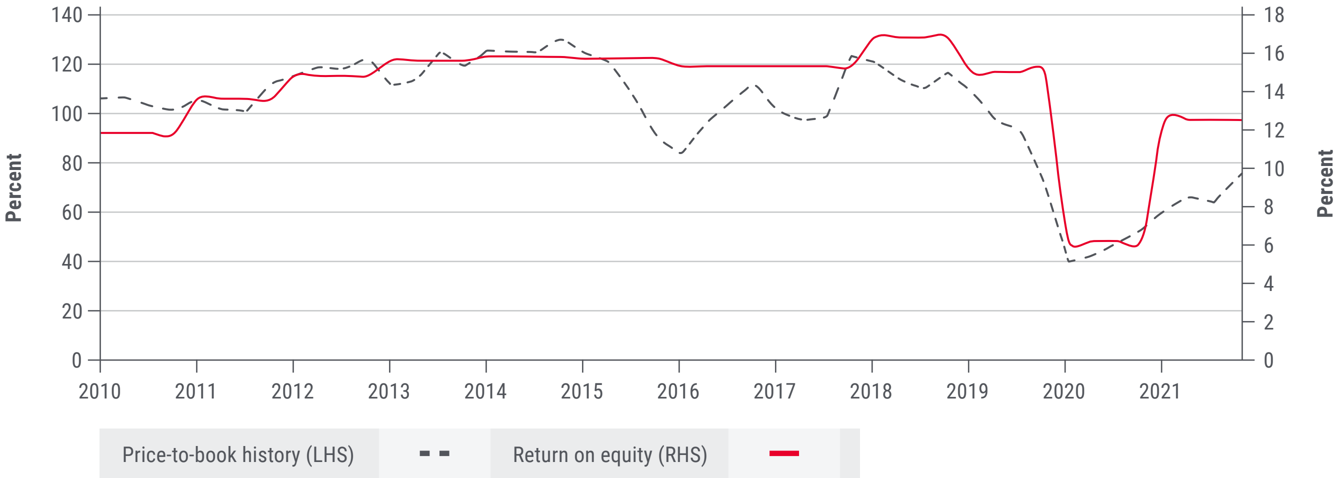
other hand, clients seem to appreciate this, as evidenced by improving customer satisfaction survey results and increased market share over the last two years.

The price you pay matters

As valuation-focused investors, we look for companies where market expectations mirror recent trends despite evidence of green shoots. While there are always tail risks associated with investing in banks, we think Nedbank-specific risks are being overpriced and that the increasing efficiency of Nedbank's retail business will likely be a driver of value.

As a simple rule of thumb, the multiple of book value that investors are willing to pay for a bank is determined by its return on equity (ROE). **Graph 4** shows how this relationship has held over time, with the price-to-book ratio shown as a percentage of the long-term average multiple. We think there is upside to current ROEs, which should drive a higher valuation multiple, with Nedbank currently trading at a discount to both its peers and its own history.

Graph 4: Price-to-book history vs. return on equity



Sources: S&P Global, company reports, Allan Gray research

Siphesihle joined Allan Gray in 2017 and is an analyst in the Investment team. He holds a Bachelor of Commerce (Honours) degree in Economics and Finance from the University of Cape Town.

ORBIS GLOBAL BALANCED: RUSSIA-UKRAINE CONFLICT ACCELERATES MARKET SHIFTS

Alec Cutler

... the conflict has accelerated shifts that had already begun – towards higher inflation, shortages in energy and commodities, a retreat from globalisation, and rising geopolitical risk.

Russia's invasion of Ukraine is a painful reminder that there is more to life than markets, and our concern goes out to the people suffering. As investors, our job is to assess the impact on our clients' portfolios. Alec Cutler, from our offshore partner, Orbis, focuses on the Orbis SICAV Global Balanced Fund.

Coming into this year, the Orbis SICAV Global Balanced Fund ("the Fund") held no Russian positions. We did hold BP, which has since walked away from its 20% stake in Rosneft, but we sold out between late January and mid-February, feeling that the Russia-related risk was underappreciated. We recycled much of the cash from BP into more attractive energy ideas.

In markets, the conflict has accelerated shifts that had already begun – towards higher inflation, shortages in energy and commodities, a retreat from globalisation, and rising geopolitical risk. We have worried about these risks for some time, and have sought to mitigate them in the Fund.

The Fund has fared much better than its 60/40 benchmark amid the conflict-related volatility. As already-high inflation has eclipsed 7% in the US, 10-year Treasury yields have risen from 1.5% in December 2021 to 2.3% today. That has punished global government bonds, which have lost 6.2%. It has also punished the richly priced growth stocks that are valued on future hopes rather than present profits. While global value shares are roughly flat this year, the Nasdaq is down 9%.

Those moves feel huge if you're reading the headlines every day. But they have barely made a dent in the trends of recent decades. Bond yields remain near 120-year lows in the US, 260-year lows in the UK, and 700-year lows globally. And over the past 15 years, the Nasdaq has only once been more richly priced relative to global value shares – and that was during the COVID-19 lockdowns.

So while our cash, gold, inflation-linked bonds and hedged equity positions have (finally) thrashed conventional bonds this year, we continue to find those assets very attractive compared to the return-free risk of long-term nominal bonds.

Similarly, owning neglected shares has worked much better than paying up for the perception of perpetual profitable growth thus far this year. We continue to believe that buying businesses for less than they are worth is the surer way to avoid losses. Will the real defensives please stand up?

Some aspects of the current environment look worse than in the 1970s ...

Bell-bottoms, government cheese and UB40s

The shifts towards higher inflation, scarcer resources, and a more divided world did not start on 24 February. Many aspects of the current environment recall the 1970s: monetary stimulus, policy experimentation, fiscal stimulus, politicians' intolerance of recession, supply-driven commodity inflation, resurgent labour, and geopolitical upheaval – all scary similarities. In that era of bell-bottoms, government cheese and UB40s, the prices of stocks and bonds went down, while the price of everything else went up. In real terms, investors in a US 60/40 portfolio got 3% poorer every year for a decade.

Some aspects of the current environment look worse than in the 1970s, despite official reassurances. Having printed money at an unprecedented rate, central bankers are now talking up their self-described "toolkits" to manage inflation. In the UK, the Bank of England's toolkit apparently includes telling workers to show "restraint" in pay bargaining. Such aloofness is not unique to the UK. In the US, Federal Reserve chair Jerome Powell has called the job market "tight to an unhealthy level", and he has drawn comparisons to Paul Volcker for his tough talk on inflation. Mr. Powell may need an orthodontist after all that jawboning – real interest rates in the US are at their most negative levels in 40 years.

Yet inflation expectations have continued to rise. That is dangerous, because inflation is unlike most financial risks. With most financial risks, the more you worry about it, the less likely it is to happen. With inflation, the more you worry about it, the more likely it is to get worse.

Three boomerangs

Inflation is not the only area where Russia's invasion has exacerbated trends that were already underway. In the Fund, we have found opportunities aligned with three of these trends: a global energy crisis, a global food shortage, and a resumption of the Cold War. Each of these represents a reversal of the prevailing trends in recent decades, and each could shape the world for decades to come.

Global energy crisis

We have expected a supply crunch in energy for some time. Over the past seven years, oil producers have underinvested to the tune of hundreds of billions of dollars, chastened by the price declines of 2014-2015, the negative prices of 2020, and growing environmental, social and governance (ESG) pressure throughout. By early February this year, oil prices had risen to US$90 a barrel, but were still not enough to coax production growth out of listed producers and their bruised shareholders. At the same time, OPEC producers with scant spare capacity are struggling to meet their own production quotas, and despite record draws from the US Strategic Petroleum Reserve, commercial petroleum inventories are at their lowest levels since 2014.

We continue to believe that buying businesses for less than they are worth is the surer way to avoid losses.

Then Russia invaded Ukraine, immediately rendering 10% of world oil production and over 30% of Europe's gas supply insecure and toxic. As the world divides between oil producers and consumers, and between consumers willing to buy from Russia and those who aren't, we look to be on the cusp of a global energy war. It is becoming obvious that the US must lead the way in providing the West, and Europe in particular, with energy security. In fact, Europe and the US have already signed an agreement to increase transatlantic liquefied natural gas (LNG) shipments.

The most obvious beneficiaries are responsible Western companies that can contribute to the energy security effort. Much of that LNG will be handled by Shell, one of the world's largest LNG producers and traders. 40% of gas consumed in the US flows through the pipelines of Kinder Morgan, which also owns stakes in LNG export terminals. As European LNG demand boosts prices in Asia, gas producers in Australia such as Woodside and Inpex will benefit. And companies like Schlumberger and Hunting, which provide the technology and equipment to increase oil and gas production, stand to benefit as countries and companies finally attempt to increase supply.

... we remain enthusiastic about the Fund's long-term relative return potential.

As obvious as all that seems, this is not reflected in valuations. Shell, Woodside and Inpex all trade at more than 20% free cash flow yields on today's US$105 per barrel oil price, and on double-digit free cash flow yields with lower long-term oil price assumptions. The share prices of Schlumberger and Hunting are 50% below their 2018 levels, despite what we see as a far brighter outlook. And Kinder Morgan offers a well-covered 5.7% dividend yield that is backed by inflation-linked "take or pay" contracts where customers must pay for pipeline volumes whether they use them or not. Over the past few months, we have rotated the Fund's energy holdings from politically vulnerable producers towards the more neglected services firms, while maintaining the overall energy exposure near 20% of the portfolio.

Longer term, the energy shortage may hasten Europe's desire to increase energy efficiency and transition to renewable power. One of the easiest efficiency wins is to use LED light bulbs, which should provide a tailwind to Signify, maker of Philips-branded LED bulbs. Yet it too offers a double-digit free cash flow yield. And investment in renewable energy should support both the wind turbine and electrical grid equipment businesses of Siemens Energy, whose stock price has languished near its lowest levels since listing in late 2020.

Global food shortage

Russia is by far the world's largest wheat exporter, and in normal times, Russia and Ukraine together account for a quarter of the world's wheat exports. As that supply is threatened, food prices have spiked globally. Replacing any lost supply will be made more difficult by high prices for potash and natural gas, two key ingredients in fertiliser production. Russia and Belarus are two of the world's largest potash producers and are constraining exports. That will make it essential for producers in other regions to maximise crop yields.

Top holding Bayer, with its world-leading portfolio of yield-enhancing seeds, fertilisers and pesticides, may be due a reappraisal. Once loathed for genetically modified seeds and Roundup (glyphosate), Bayer now seems utterly forgotten, even as its Roundup legal fortunes improve. As it dawns on countries that food can be scarce, Bayer should enjoy healthy demand for its products, yet it trades for less than 10 times earnings. Nufarm, a smaller Australia-listed agribusiness, should enjoy similar tailwinds.

The Fund also gains some protection against rising food prices through its Treasury Inflation Protected Securities. The principal value of these bonds adjusts according to changes in consumer prices, and food and energy account for roughly a quarter of the consumer price basket.

Amid all the volatility of recent months, we have resisted the urge to trim positions that have performed well ...

The Cold War resumes

With Russia's invasion of Ukraine, the era of predictable European and Asian peace that started in the early 1990s is now well and truly eliminated – along with all of the economic blessings that came with it. With the peace dividend gone, countries and alliances need to make up for a decades-long investment deficit in defence. That need is being felt most acutely in Europe and Japan, where defence contractors have performed poorly for 20 years, recently exacerbated by investor unease about the social responsibility of investing in those firms. Now, we appear to be on the cusp of a boomerang-like turn in both fundamentals and sentiment.

On the fundamental side, European powers are already ramping up defence spending, and are favouring local contractors such as BAE Systems, Saab, Rheinmetall, Rolls-Royce, Leonardo and Thales. Japan and Mitsubishi Heavy, the maker of Japan's military ships and aircraft, are experiencing a similar dynamic. Together these represent over 4% of the Fund following their recent outperformance. Most offer high dividend yields that are well covered by cash flows on current contracts, with additional upside should defence spending increase. And on the sentiment side, investors are reassessing the importance of defence companies in protecting liberal democracies.

We did not buy these companies because we foresaw events in Ukraine. But as relations between former Cold War rivals have gone from tepid, to cool, to frosty over recent years, we believed rising geopolitical risks were not reflected in their valuations, and we had been slowly building positions for several months. At the end of January, before the conflict, these shares represented 2.5% of the Fund.

A yawning gap

Amid all the volatility of recent months, we have resisted the urge to trim positions that have performed well in favour of shares that have recently started to lag. In our view, the boomerang in markets has only started to turn, and the much-discussed “value rotation” is mainly a sell-off in shares that looked absurdly expensive before and still look extreme.

After a good quarter for relative returns, the equities in the Fund still trade at a 30% discount to the MSCI World Index on price-to-earnings, and a 40% discount on a free cash flow basis. Accordingly, we remain enthusiastic about the Fund’s long-term relative return potential.

Invest Differently

Alec joined Orbis in 2004. He is a member of the Bermuda-based Multi-Asset Investment team and is responsible for the Orbis Global Balanced Strategy. Alec holds a Bachelor of Science (Honours) degree in Naval Architecture from the United States Naval Academy and a Master of Business Administration from The Wharton School of the University of Pennsylvania. He is also a CFA® charterholder.

IS THERE VALUE IN OUR INVESTMENT STYLE?

Grant Pitt

… our flexible approach enables us to take advantage of whatever types of opportunities the market presents.

Understanding your investment manager's style may give you a deeper appreciation of how they will perform in different circumstances, and therefore help you understand the type of risk you are taking on as well as the performance potential. Curious clients often ask where we sit on the style spectrum; we prefer not to box ourselves in. Grant Pitt discusses why.

Investment style is one of the aspects of investing used to describe an investment manager's investment philosophy and approach. In essence, the "style" determines the subset of shares a manager will consider in their stock selection process and can therefore be a useful differentiator between managers. If a manager's style resonates with you, and you take the time to understand it, you are more likely to stay the course and benefit over the long term.

But as with many things in life, labels can help, but sometimes fail to capture the full picture. People often refer to Allan Gray and Orbis as "value" managers. To unpack whether this statement holds true, and the label is relevant, we will first define "value investing" and then take a look at some of the data to see if it applies.

What is value investing?

The concept of value investing was first introduced in business schools in the 1920s by Benjamin Graham and David Dodd. Graham later went on to publish the highly acclaimed *The Intelligent Investor* in 1949, and today is widely considered the father of value investing. Graham suggested that investors should look for discrepancies between the market price of a share and its true intrinsic value, while providing for a margin of safety, or room for human error. He maintained that market prices are often not to be relied on given the human emotions driving those prices.

Interestingly, Graham never actually used the phrase "value investing"; the term was later coined to describe Graham's ideas. However, as many of the early opportunities identified by Graham and Dodd were shares trading on low price-to-earnings or price-to-book valuation multiples, it has led to a misinterpretation of his principles, with most now considering value investing as investing in shares that trade on low valuation multiples.

Growth investing, in contrast, seeks to invest in shares that offer superior earnings growth potential to the average company, and which therefore often trade at an above-average valuation multiple (whether price-to-earnings, dividend yield or price-to-book metric).

Shares are … included when they offer superior expected risk-adjusted returns to the market.

How do we define our investment style?

At Allan Gray and Orbis, we consider ourselves "value-orientated" investors – very much in the Benjamin Graham mould. As Allan Gray himself noted in the June 1996 Orbis Global Equity Fund quarterly report:

"We aim to buy a participation in a business on your behalf at a market price which is well below what our research leads us to believe is its intrinsic value. This stems from our conviction that this offers the best prospect of superior returns and below average risk of loss. We favour investing in companies which we expect to experience above-average growth in earnings per share for the foreseeable future. However, we prefer not to pay 'over the odds' for such superior prospective growth …"

It should not come as a surprise, then, that Graham's illustration of the "margin of safety" principle looks very similar to how we (Allan Gray and Orbis) depict our shared investment philosophy.

Although we have never limited our search to shares trading at low price-to-earnings or low price-to-book multiples, our contrarian investment philosophy naturally leads us to out-of-favour areas of the market and shares that, on average, trade at depressed multiples relative to the broader market. However, we do not limit our research to fast or slow growth, high or low quality, big or small companies, and we don't avoid shares simply because they trade on high valuation multiples. Like Graham, we aim to identify shares that trade significantly below what we think they are truly worth today, factoring in the expected future growth potential.

What does the data reflect?

In **Graphs 1a** and **1b**, we have classified the shares within the South African market according to their value and growth characteristics. Each circle in Graph 1a represents a constituent share on the FTSE/JSE All Share Index (ALSI) as at the end of February 2022.

Shares are classified on the horizontal axis according to their valuation – the further to the right, the more expensive they are. The vertical axis classifies shares by their cyclicality (how volatile their prices have been on a relative basis). The higher the share, the more cyclical it has been historically[1]; the lower the share, the more defensive (having less variability in price fluctuations). As the valuations and cyclicality/defensiveness metrics are relative calculations, one would expect a relatively even distribution across the spectrum, or four quadrants, as reflected in Graph 1b[2].

Great investment opportunities can be found in any market environment.

However, what Graphs 1a and 1b fail to capture is that not all constituent shares within the market carry an equal weighting. The ALSI is relatively concentrated, so accounting for the divergent market capitalisations of companies – reflected by the size of the grey bubbles in **Graph 2a** on page 20 – the picture looks somewhat different. The local shares held within the Allan Gray Equity Fund ("the Equity Fund") have also been included (the red bubbles) and reflect the different positioning of the Equity Fund to the market. The numerical weightings per "style" are reflected in **Graph 2b** on page 20 – the Equity Fund in red and the ALSI in grey.

What may surprise those who think of us as a "value" manager is that growth shares actually account for more than half of the Equity Fund today (53%), while value accounts for 47%,

---

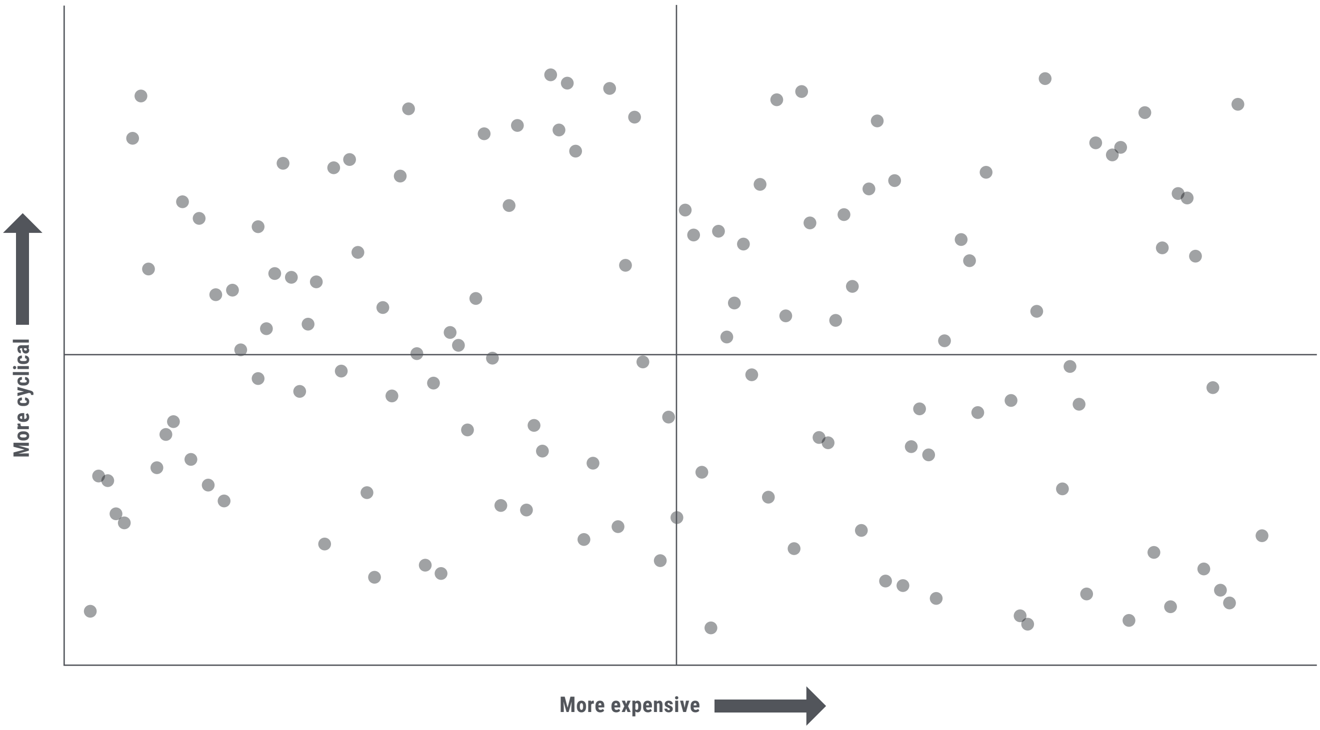
[1] Statistics are compiled from internal research databases and are subject to subsequent revision due to changes in methodology or data cleaning. Each circle represents a constituent stock of the FTSE/JSE All Share Index (ALSI). Stocks in the ALSI are ranked based on their valuations (normalised earnings yield, free cash flow yield and book to price, based on trailing 12-month fundamentals) and their volatility relative to a basket of bond yields (as a proxy for cyclicality).
[2] Nine recently listed or unbundled shares that don't have valid volatility metrics have been excluded, which results in the imbalance across the quadrants.

with the distribution across the four quadrants relatively even. From a market viewpoint, growth shares represent almost two-thirds of the market (64%), with value representing only 36%.

Delving further, the Equity Fund is overweight value/defensive (+11%), marginally overweight growth/defensive (+1%), equal weight value/cyclical, and underweight growth/cyclical (-12%), despite it comprising the largest component of the Equity Fund (31%). The four largest shares in the Equity Fund as at the end of February 2022 are also highlighted, and interestingly, each falls into a different quadrant.

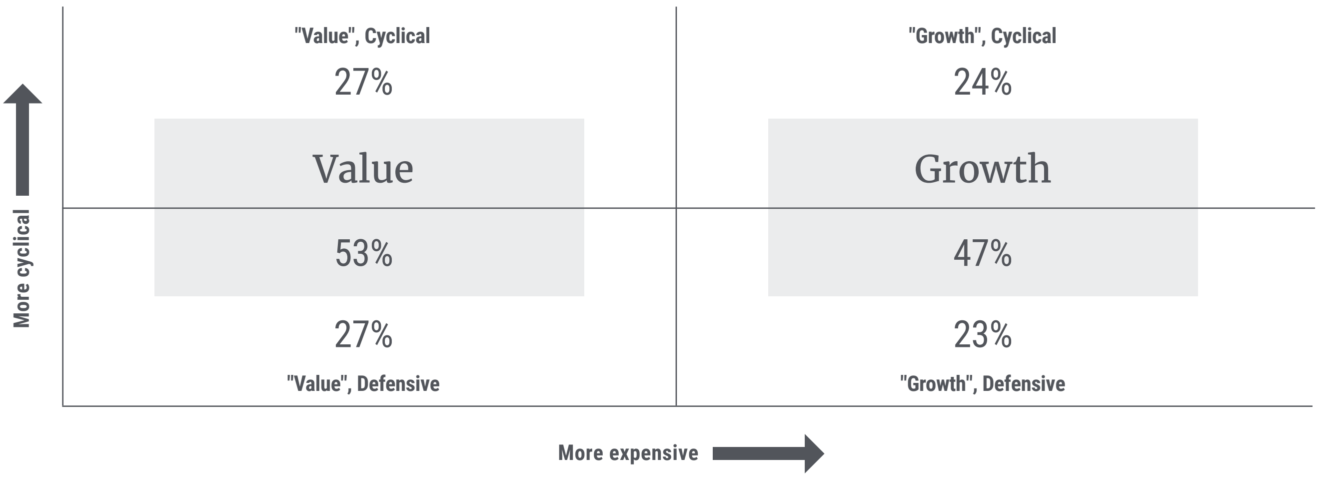
Markets are dynamic and share prices fluctuate, occasionally aggressively so, as we have witnessed in the first quarter

Graph 1a: Equal-weighted ALSI – under the microscope (Feb 2022)



Source: Allan Gray research

Graph 1b: Equal-weighted ALSI – numerical spread (Feb 2022)

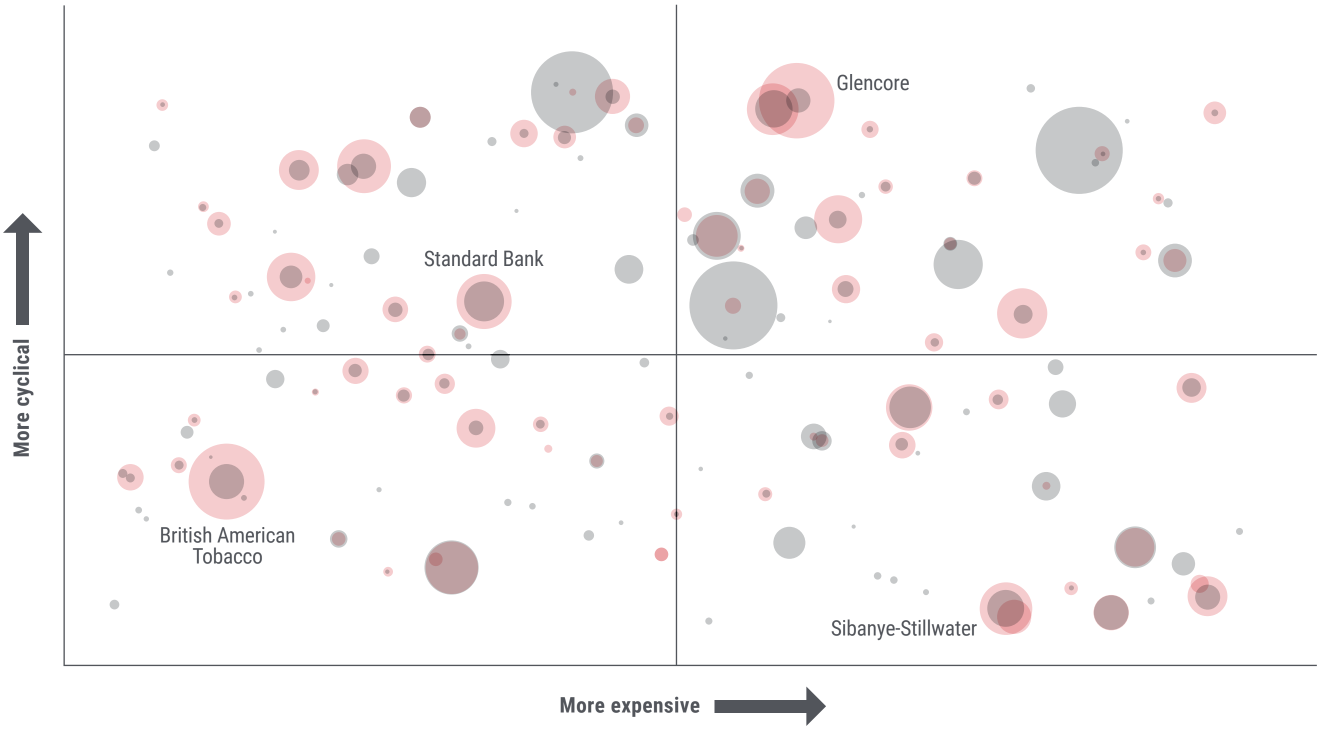


Source: Allan Gray research

of 2022. The relative attractiveness of shares therefore varies over time and shares can move between quadrants based on price movements. For example, British American Tobacco today is classified as value/defensive, whereas a few years ago it would have been classified as growth/ defensive. One should therefore expect the exposure per quadrant to vary as the opportunity set evolves.

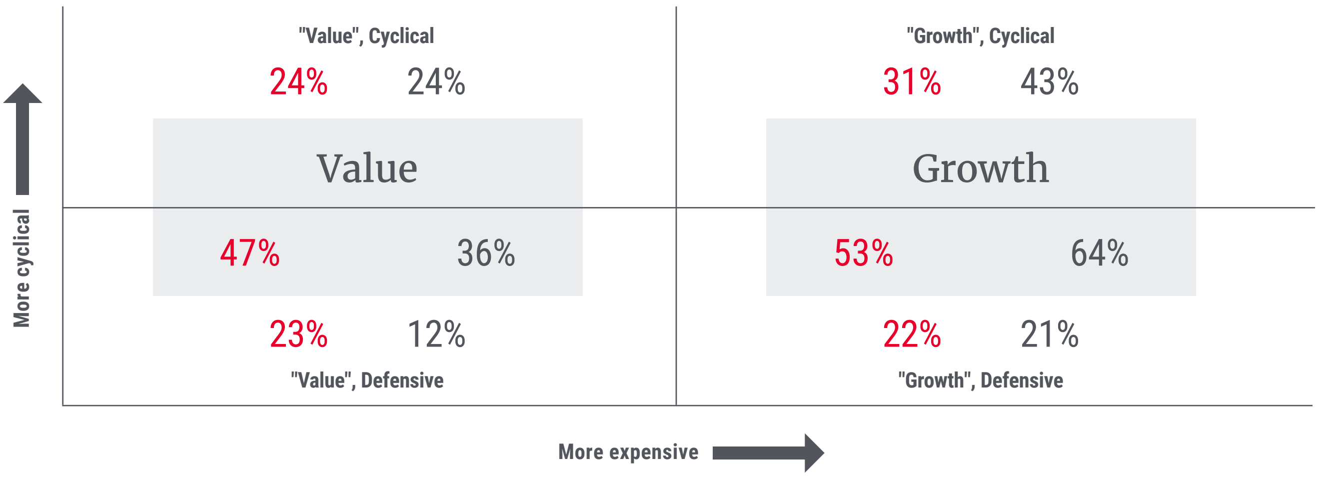
This can be seen if we consider the market five years ago, as reflected in **Graphs 3a** and **3b**. In February 2017, there was more balance between growth and value (56% vs. 44%) than what we see today. At the time, the Equity Fund still had slightly more exposure to growth (52%) and was less overweight value relative to the market (+4% vs. +11% currently). In contrast to today, we were finding greater

Graph 2a: Market cap-weighted ALSI and Allan Gray Equity Fund – under the microscope (Feb 2022)



Sources: Allan Gray, Orbis research

Graph 2b: Market cap-weighted ALSI and Allan Gray Equity Fund – numerical weightings (Feb 2022)



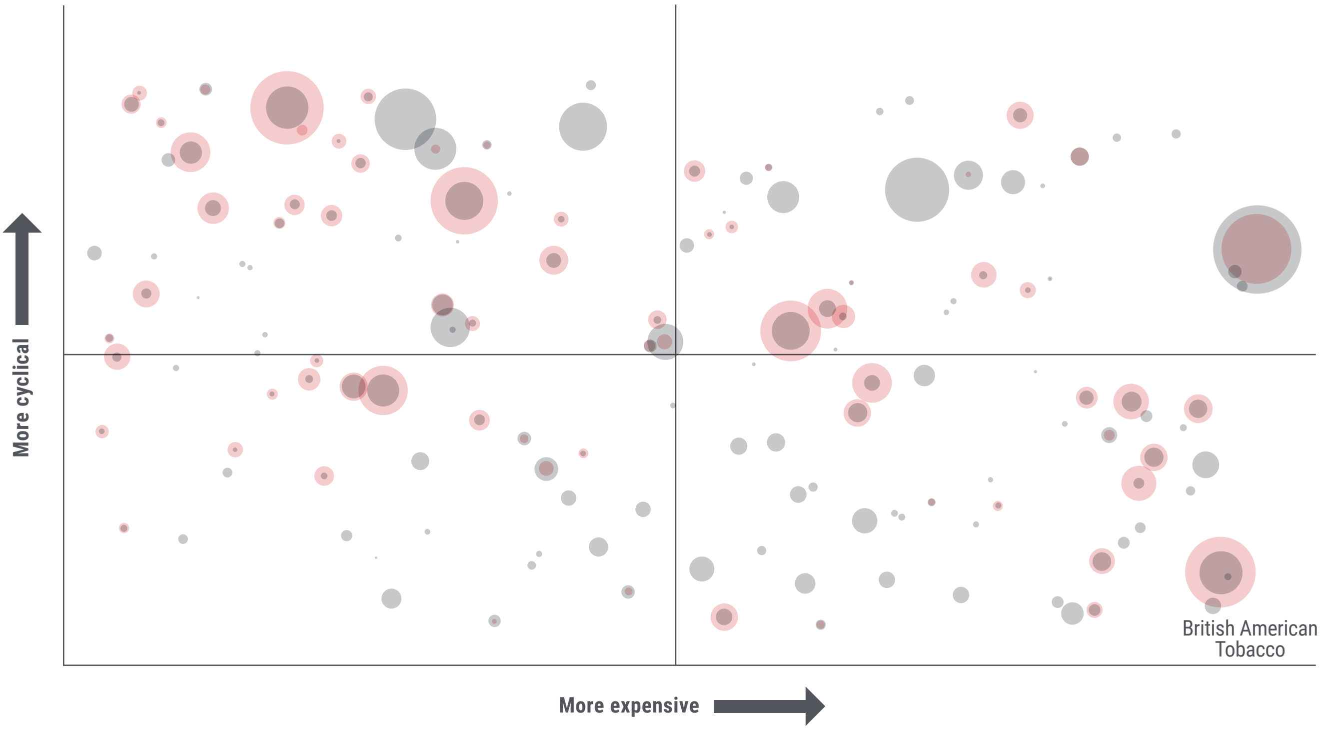
Sources: Allan Gray, Orbis research

value in growth/defensive (+4%), fewer relative opportunities in the value/defensive bucket (+2%) and were less underweight growth/cyclical (-8%).

It is important to highlight that this historical analysis does not have any influence on how we construct portfolios.

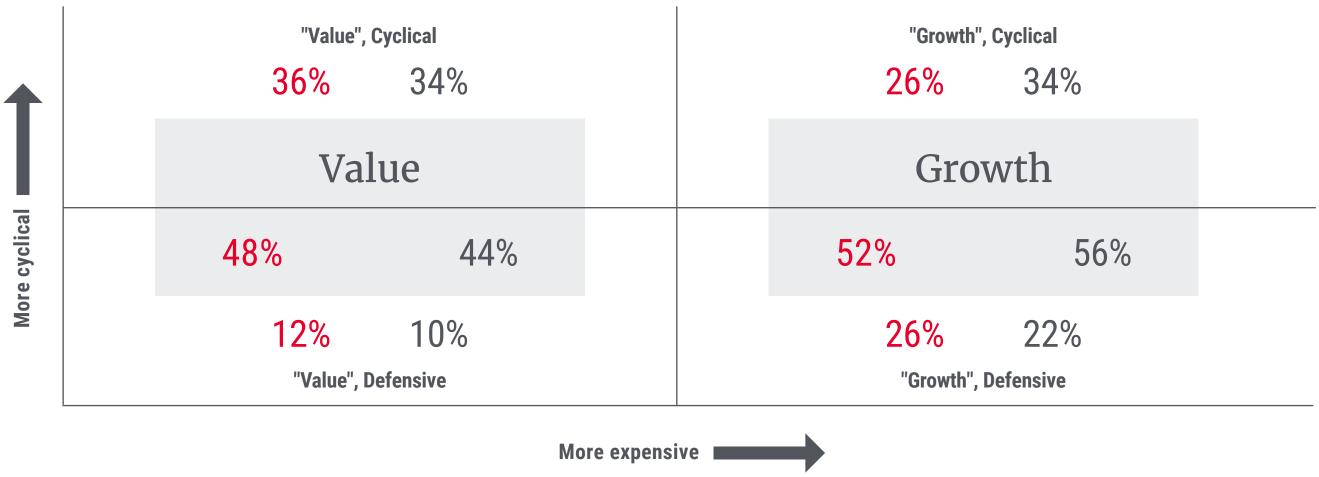
Shares are identified through our bottom-up, fundamental research process and included when they offer superior expected risk-adjusted returns to the market. If several individual opportunities are identified which happen to fit a certain style, then it is likely that the Equity Fund will have meaningful exposure to that style at a point in time.

Graph 3a: Market cap-weighted ALSI and Allan Gray Equity Fund – under the microscope (Feb 2017)



Sources: Allan Gray, Orbis research

Graph 3b: Market cap-weighted ALSI and Allan Gray Equity Fund – numerical weightings (Feb 2017)



Sources: Allan Gray, Orbis research

Avoid getting tangled in the theory

While it is popular to try to distinguish between value and growth investing, we maintain that it is misleading to do so. This is partly because growth potential is one of the essential inputs required to calculate intrinsic value, and calculating intrinsic value is key to value investing.

Warren Buffett expressed this sentiment in his 1992 chairman's letter, in which he made it clear that growth is always a component in the calculation of value – i.e. it makes no sense to choose between value and growth:

"But how, you will ask, does one decide what's 'attractive'? In answering this question, most analysts feel they must choose between two approaches customarily thought to be in opposition: 'value' and 'growth.' Indeed, many investment professionals see any mixing of the two terms as a form of intellectual cross-dressing.

… In our opinion, the two approaches are joined at the hip: Growth is always a component in the calculation of value, constituting a variable whose importance can range from negligible to enormous and whose impact can be negative as well as positive."

Great investment opportunities can be found in any market environment. We are opportunistic, and our flexible approach enables us to take advantage of whatever types of opportunities the market presents. We believe this is in the best interest of our clients, even if it may frustrate those who want to simplify the categorisation of our investment style.

Grant is head of the Institutional Clients team. He joined Allan Gray in 2009 as an investment analyst after working for several years in financial services in the UK. Grant holds a Bachelor of Business Science degree from the University of Cape Town and is a qualified Chartered Accountant and a CFA® charterholder.

SHOULD I INVEST 45% OF MY PORTFOLIO OFFSHORE?

Earl Van Zyl

... the ideal level of offshore allocation over the long term depends on your specific circumstances and investment goals.

In the February 2022 Budget speech, the National Treasury announced significant changes to the framework that governs how much of South African retirement savers' portfolios can be invested outside South Africa, opening the door for additional foreign exposure. This is positive for South African investors over the long term, as it allows for greater diversification and flexibility to benefit from the global opportunity set. But should you use the full allocation right now? Earl Van Zyl investigates.

Retirement and local unit trust investors are now able to allocate up to 45% of their portfolios anywhere outside South Africa, from the previous offshore limits that allowed 30% outside Africa, plus 10% in Africa excluding South Africa ("ex-SA"), for a theoretical maximum of 40%. While the increase in the total allowed outside South Africa on paper is only five percentage points, in reality, most investors previously held less than 5% in Africa ex-SA. In practice, the recent change will mean that most investors can now invest an additional 50% of their portfolio offshore.

Why is offshore investing important?

Put simply, the ability to allocate to offshore markets presents long-term investors with an opportunity to better diversify the risk exposure of their investment portfolios and to enhance returns so that they reach retirement with a larger savings pot. Of course, diversification isn't simply about going offshore; as with local investing, investors should consider blending asset classes that typically do not move in sync (i.e. their returns are not perfectly correlated) so that portfolio returns are protected when one asset class performs poorly and higher returns should come from other parts of the market, which should make it easier for investors to stay the course.

Table 1 on page 24 shows the correlation between real returns for South African and global equities and bonds over the last 30 years.

Here we see that having a portfolio that is diversified across the major asset classes is likely to be a good approach over the long term, as no asset class is perfectly correlated with another, as one would expect. However, the key insight from this table is that there are benefits to allocating offshore both within one's equity portfolio and one's bond portfolio over the long term. South African

Table 1: Correlation* between annual returns for different asset classes (1992–2021)

	SA equity	SA bonds	Global equity
SA equity	1.00	–	–
SA bonds	0.21	1.00	–
Global equity	0.34	−0.03	1.00
Global bonds	−0.31	0.06	0.43

*A positive correlation means that the variation in two asset classes is in the same direction. A negative correlation means that the variation in asset classes is in opposite directions. Correlation can vary from -1 to 1.
Sources: DMS and Morningstar data, Allan Gray analysis

equities and bonds had a low correlation with their global equivalents, and an even lower correlation across asset classes – e.g. South African equities had a correlation of 0.34 with global equities and -0.31 with global bonds.

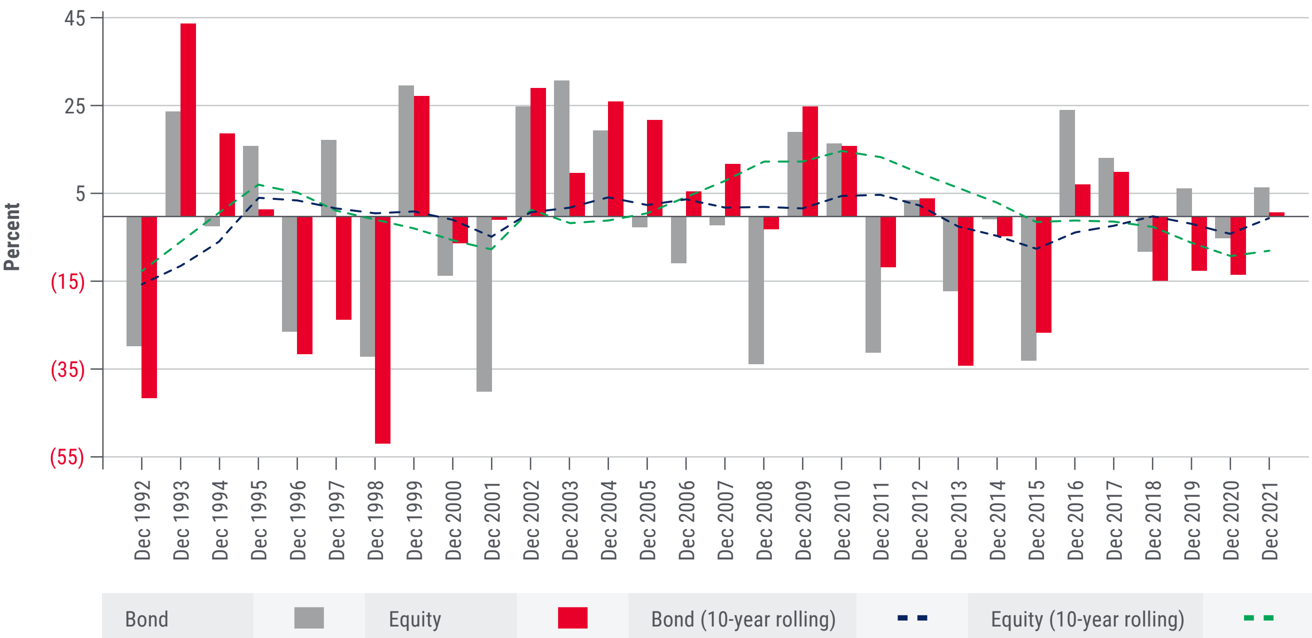
From the discussion so far, we can say that diversification away from one's home market is a valuable portfolio construction tool that most investors should be using.

Graph 1 shows the difference (or excess) in annualised real returns (in rands) between South African and global asset classes delivered up to the end of 2021, summarised annually (bars) and over a rolling 10-year period (lines) for the last 30 years.

As the graph illustrates, excess returns are cyclical, with South African equities having generated sustained excess returns versus global equities from 1993-95, 2002-07, 2009-10 and 2016-17. Although excess returns in 2021 were 0.9%, over 10 years investors would still have been worse off by 8% per year had they invested only in South African equities versus entirely in offshore equities. Excess returns from bonds have been similarly cyclical, though within a narrower range over most of the period.

The outcome in equities excess returns over the last five years provides some evidence for the rhetoric in the media over the recent past about investing offshore rather than in South Africa. However, as we have already noted,

Graph 1: Excess* real returns of South African assets vs. global assets



*Excess returns, here, is used to mean the difference between South African and global asset returns.
Sources: DMS and Morningstar returns, Allan Gray analysis

investing is cyclical, and decisions today about how much of your portfolio should be invested offshore, and into which offshore assets, should not be made with simple extrapolations from the past into the future. Nevertheless, the long-term data bears out that investing offshore improves portfolio diversification over time and enhances the opportunity set for generating real returns.

How much should one invest offshore?

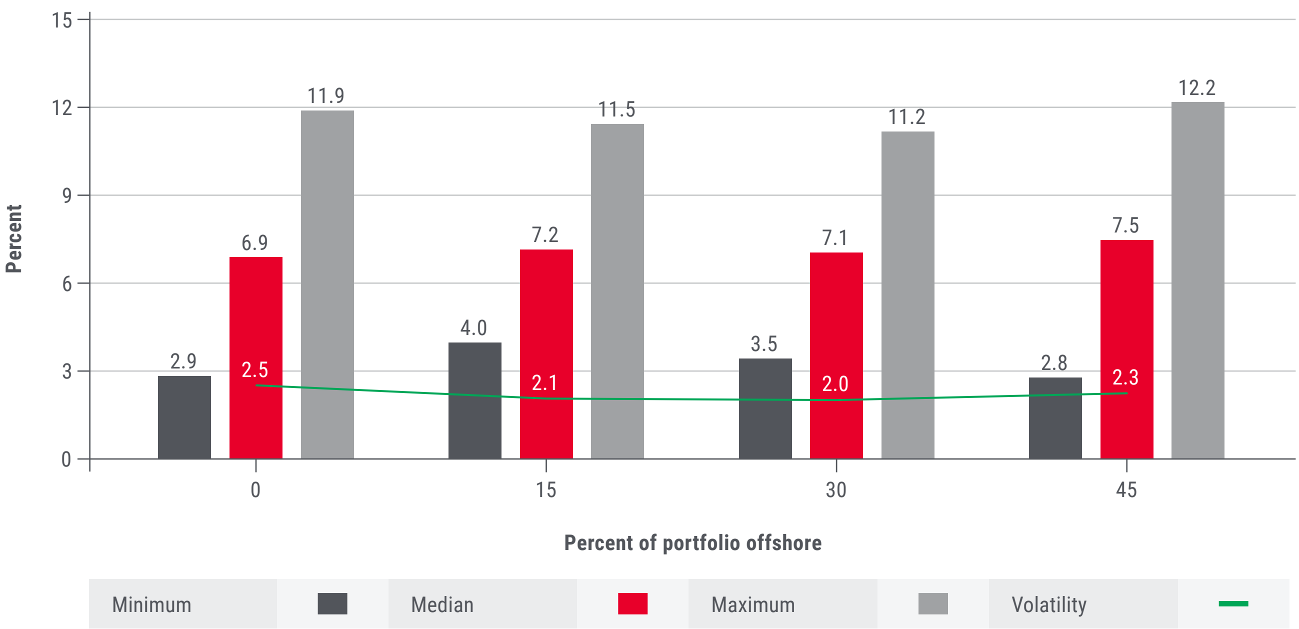
As with most questions in investing, the answer depends on your personal circumstances, risk appetite and required real return. For simplicity, we will illustrate the factors to consider, and the trade-offs to be made, using a simplified but representative multi-asset portfolio blend of 60% in equities and 40% in bonds, which would have delivered 10-year annualised real returns of 6.9% on average over the last 30 years if invested entirely in South African assets. We will assume that as the portfolio allocates more offshore, there is an equal allocation between equities and bonds offshore – that is, 30% offshore means that 30% of the equity portfolio and 30% of the bond portfolio is invested offshore.

Graph 2 illustrates that allocating a higher proportion of one's portfolio offshore has a meaningful impact on the expected outcome of that portfolio in a number of ways. Firstly, the volatility of long-term returns of the portfolio reduces as one increases the offshore allocation from 0% to 30%, and increases again at an allocation of 45%. Secondly, the average 10-year returns available from the hypothetical portfolio increase with increasing levels of offshore allocation, although perhaps less than one might have expected given the underperformance of South African equities in the recent past. Finally, the range of return outcomes narrows at offshore allocations between 15% to 30%, but is higher both at 0% offshore as well as at 45% offshore.

... there are trade-offs that investors need to weigh up to determine what allocation best meets their investment goals and appetite for risk.

These results indicate that offshore investing is not a simple matter of maximising your allocation to offshore assets. Rather, there are trade-offs that investors need to weigh up

Graph 2: 10-year annualised risk and real returns of hypothetical portfolio at different levels of offshore allocation



Sources: DMS and Morningstar data, Allan Gray analysis to determine what allocation best meets their investment goals and appetite for risk.

Some readers may argue that negative excess returns of South African equities versus global equities over the last five years suggest that our simplified model is flawed; that perhaps South African investors should be using most of their offshore allocation for equities, rather than a similar blend of equities and bonds to the local component, especially as expected real returns from South African bonds today are extremely attractive in absolute terms and relative to global bonds.

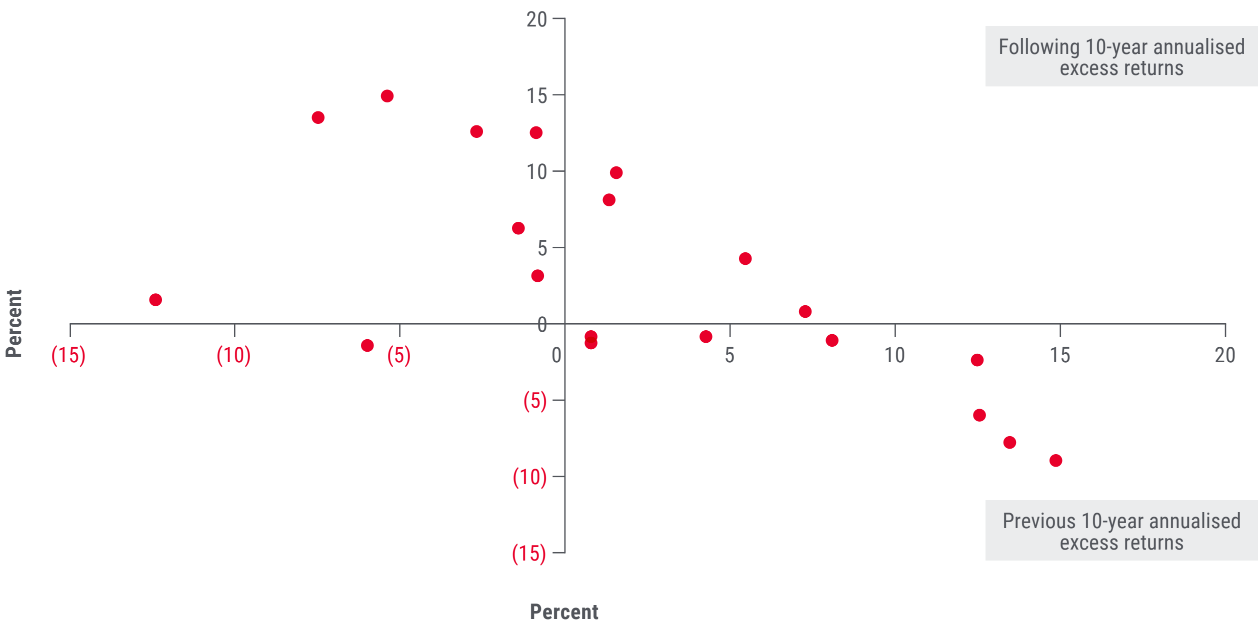
However, this argument would be dangerously reliant on the next 10 years looking like the last 10. In **Graph 3**, we plot the relationship between past (horizontal axis) and future (vertical axis) equities excess returns, again using data from the last 30 years.

The graph shows that there is strong evidence that when 10-year excess returns from South African equities versus global equities were negative, as they are today, the following 10 years most often – though not always – saw South African equities generating positive excess returns. This is another way to make the point that returns are cyclical, as are excess returns, and that periods of over- or underperformance are often followed by periods of under- and overperformance respectively.

Another important factor to consider as you increase your offshore exposure is the volatility of the rand exchange rate versus those of global currencies. The rand is one of the most tradeable emerging market currencies, and also one of the most volatile. **Graph 4** shows the volatility of the rand-US dollar exchange rate over the last 21 years. Although the average volatility over the whole time frame was 13%, there were periods when the volatility of the exchange rate was much higher, often coinciding with higher market volatility in general, which increases the volatility of the investment portfolio when investing in rands.

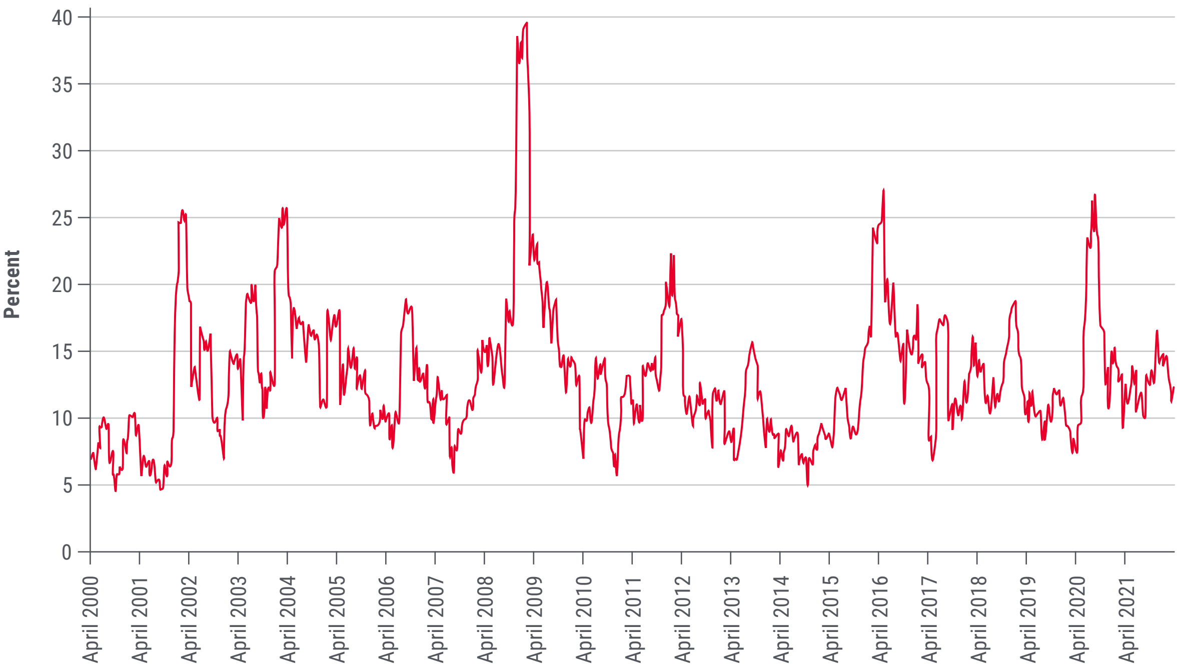
How to account for this risk will be different for investors contributing to their retirement portfolio, for example through monthly contributions, and those investors purchasing a living annuity at retirement and earning a monthly income in rands from their investment. This is not to suggest that you should try to avoid this currency risk. The risk and return data that we have already discussed includes the effects of exchange rate volatility. Rather, it is important to be aware that exchange rate volatility takes on increasing significance in your portfolio as you increase your allocation offshore and depending on

Graph 3: Following 10-year excess equity returns vs. previous 10-year excess equity returns



Sources: DMS and Morningstar data, Allan Gray analysis

Graph 4: Annualised weekly volatility of rand-US dollar exchange rate



Source: Allan Gray analysis

whether you are contributing to your portfolio or drawing an income from your portfolio.

Key takeaways

Many clients have been asking whether or not to take full advantage of the increased offshore allocation now allowed under regulation. As discussed, the ideal level of offshore allocation over the long term depends on your specific circumstances and investment goals. A good, independent financial adviser can help you to work out what is the most appropriate exposure for you, and how this should vary depending on whether you are saving for retirement or are already in retirement and earning an income from your accumulated investments.

In managing Allan Gray's Equity, Balanced and Stable funds, our investment team continues to assess this question, as they always have. We have been saying for some time that South African assets currently offer better value than many of their offshore counterparts, so we are not allocating more offshore simply because the regulations allow us to do so. Instead, our portfolio managers will continue to make decisions about the level of offshore exposure according to our assessment of where the best value can be found over the long term. Investing in an asset allocation fund that is appropriate for your risk appetite can take the pressure off you having to make your own decisions in this regard.

Earl joined Allan Gray in 2015 as a manager in Product Development, spent two years leading our Digital teams, and currently heads up the Product Development team. He holds a Master of Business Administration from the University of Chicago Booth School of Business and a Bachelor of Science degree in Aeronautical Engineering from the University of the Witwatersrand.

HOW SARS HAS CHANGED TAX FOR ANNUITANTS

Carrie Norden

This change may impact taxpayers who receive annuity income from more than one provider and/or those who receive a salary and annuity income.

The South African Revenue Service recently changed the way tax is calculated for living annuitants. Carrie Norden discusses the rationale behind this change and the impact it may have on your take-home living annuity income.

A change introduced by the South African Revenue Service (SARS) came into effect on 1 March 2022, requiring annuity providers, including Allan Gray, to withhold a fixed tax rate higher than the rate we apply based on the personal income tax table, for some clients' Allan Gray Living Annuity income from the 2022/2023 tax year. The change aims to reduce the tax shortfall clients may face at the end of the tax year by applying fixed tax rates calculated by SARS (which considers the multiple sources of income they may receive) to living annuity income.

What has changed?

Tax on living annuities is a pay-as-you-earn (PAYE) tax that is withheld by an annuity provider according to the tax rate prescribed by the personal income tax table, taking the annual tax rebates into account. Until recently, annuity providers have withheld tax as if the annuity (or annuities) under their administration were their clients' sole source of income. Annuitants can instruct their annuity provider to apply a higher tax rate and withhold additional PAYE tax from their annuity income if they wish to compensate for different sources of income. Some taxpayers may also hold a reduced-rate directive issued by SARS (to deduct or withhold a lower rate of PAYE tax) for the tax year. This may be, for example, to alleviate hardship due to circumstances outside the taxpayer's control, or the directive may be issued to avoid double taxation.

As of 1 March 2022, annuity providers will be required to withhold tax for select living annuity clients at a rate that is determined by SARS considering multiple sources of income. For these clients, SARS will instruct annuity providers on the rate to use via a fixed-rate tax directive. Taxpayers may still instruct their annuity providers to apply a higher effective tax rate to their annuity income, and reduced-rate tax directives issued by SARS for the current tax year will supersede the new fixed-rate directives.

This change may impact taxpayers who receive annuity income from more than one provider and/or those who receive a salary and annuity income.

Why has this been done?

Consider a taxpayer who earns a salary from their employer and receives a monthly annuity income from their Allan Gray Living Annuity. Both their employer and Allan Gray will deduct PAYE tax from the income they administer, which is calculated by applying the personal income tax table and annual tax rebates to that income to determine how much PAYE tax to withhold and pay over to SARS on the taxpayer's behalf. As the employer and Allan Gray do not have sight of the income the taxpayer receives from the other party, they calculate the PAYE tax liability based on the income they administer, and each party applies the annual tax rebates, when this should only be applied once per taxpayer per tax year.

When a taxpayer files their tax return at the end of the tax year, SARS looks at *all* income earned during the year. In this example, in addition to the annual tax rebates being applied twice, the salary and living annuity income combined may push the taxpayer into a higher personal income tax bracket with a higher effective tax rate than that calculated by each income provider. SARS will calculate the overall tax liability when assessing the taxpayer at the end of the tax year and will deduct the PAYE tax that the employer and Allan Gray withheld throughout the year to determine if there is any difference. If the calculated PAYE tax due exceeds that which the employer and Allan Gray withheld during the year, the taxpayer will be required to pay in the additional tax on assessment. They may not be expecting this additional tax liability, nor have budgeted for it, as they may have assumed that each income provider withheld the required amount of PAYE tax from the income they paid.

Although taxpayers are able to instruct annuity providers to apply a higher effective rate that takes multiple income sources into account, not many make use of this solution. Some are unaware that this scenario may lead to a tax shortfall on assessment; others may have difficulty calculating their overall tax liability, or may not know that this option exists.

How have these rates been calculated?

The fixed tax rates issued to annuity providers have been calculated by SARS based on the latest available data they have from employers and annuity providers. In calculating the fixed tax rates, SARS took all sources of income, as well as the annual tax rebates, any retirement fund contributions, and medical tax credits into account. The rates were updated in March 2022 to take the updated 2022/2023 personal income tax table and annual tax rebates into account.

It is important to note that SARS only took employment income into account in the calculation of the fixed tax rates (such as salary income and living annuity income) and did not consider other income sources, such as rental or interest income. This means that if you earn income from other sources in addition to employment income, you may still need to pay tax over to SARS when you file your return at the end of the tax year.

This change from 1 March 2022 does not affect salary income, and the PAYE tax withheld by your employer will not be impacted; only annuity income will be impacted. Going forward, annuity providers will receive updated tax directive lists from SARS annually to be applied to the annuity income they administer for the applicable tax year.

> This change … does not affect salary income, and the PAYE tax withheld by your employer will not be impacted; only annuity income will be impacted.

Am I impacted, and what if I opt out?

If you are a provisional taxpayer (earn income other than employment income), it is unlikely that you will be impacted by this change, in other words, it is unlikely that SARS would have issued a fixed-rate directive in relation to your annuity income. This is because provisional taxpayers estimate and prepay their tax liability for the year, and can settle any shortfall in PAYE tax relating to their annuity income through the provisional payment process.

If you appeared on the SARS fixed-rate tax directive list that Allan Gray received, we would have communicated the tax rate that SARS has instructed us to apply to your living annuity income for the current (2022/2023) tax year to you.

You can elect not to have the SARS fixed tax rate applied to your annuity income. If you opt out of the SARS fixed tax rate, we will calculate the PAYE tax we withhold as we have done previously, in other words, as if your Allan Gray Living Annuity income payments were your only source of income. You can opt out of the SARS fixed rate at any point throughout the tax year, which is helpful to know if your circumstances change (for example, if you change your income drawdown percentage on your next anniversary date), or if you find you are unable to sustain the additional upfront tax liability during the year.

You can opt out of the SARS fixed rate at any point throughout the tax year …

Before deciding whether or not to opt out of the fixed rate, we recommend that you perform your own calculations, taking your multiple sources of income into account, to determine whether the SARS fixed tax rate to be applied to your annuity income for the 2022/2023 tax year is suitable, or you feel it is too high (which will result in a refund on assessment) or low (which will still result in an additional tax liability on assessment). These calculations can be complicated and contain many moving parts. If you have appointed a financial adviser and/or tax practitioner to assist with your tax matters, it is important that you consult them so that they can advise you on the best course of action, taking all your individual factors into consideration.

It may be helpful to look at the effective tax rate you paid for the previous (2021/2022) tax year to give you a sense of the impact of the higher effective tax rate on your take-home annuity income, and whether you are able to afford to pay this additional tax liability upfront or prefer to settle any additional tax liability at the end of the tax year.

Also consider expected tax deductions and rebates for the current tax year, such as retirement fund contributions and medical tax credits, in your calculations. While SARS took retirement fund contributions and medical tax credits into account in calculating the fixed tax rate, these values were based on the latest data available to SARS. Therefore, if you have since increased or plan on increasing your retirement fund contributions, for example, or expect to benefit from an additional medical expenses tax credit this tax year, this may offset some of the additional tax liability. Additionally, if you have excess retirement fund contributions on record with SARS, these will be applied on assessment to reduce the taxable portion of your annuity income, which may also result in a reduced PAYE tax liability and refund.

As an annuity provider, we do not have in-depth insight into how SARS performed the calculations to arrive at the taxpayer-specific fixed tax rates for the 2022/2023 tax year. If you, your financial adviser and/or tax practitioner have any questions or concerns regarding the SARS fixed tax rate, we encourage you to contact SARS for more detail and assistance. Remember that you can opt out if you are concerned about the accuracy of the SARS fixed rate, or while you wait for feedback from SARS on any questions you may have.

It is important to understand the impact of the SARS fixed tax rate on your cash flow, and to be aware of your options.

Carrie joined Allan Gray as an operations consultant in 2008 and is currently a senior tax specialist. She holds a Bachelor of Business Science (Honours) degree in Finance and a Master of Philosophy degree in Tax Law, both from the University of Cape Town. Carrie is also a CFP® professional.

SHOULD RULES OF THUMB BE USED TO PLAN FOR RETIREMENT?

Thandi Skade

... in investing, rules of thumb should always be considered with a pinch of salt.

There are several rules of thumb that are referred to in investing. Many of them have become widely accepted standards for determining how much to save for retirement, how much income to draw down during retirement, and how assets should be allocated during different life stages. But do these rules of thumb hold true for you on an individual level? Thandi Skade explores this proposition.

Each day, we are confronted with problems to solve and faced with hundreds of decisions that need to be made – some that can be taken on the fly and others that require more careful consideration. Rules of thumb, or heuristics, as behavioural scientists refer to them, are useful mental shortcuts that simplify complicated matters and reduce the amount of time it takes us to make decisions.

In the context of investing, rules of thumb can help guide the way we think about and approach important life considerations, like setting financial goals and planning for a comfortable retirement. However, as we illustrate with a few examples below, rules of thumb should not be considered hard and fast instructions, but rather broad and general guidelines.

Examples of rules of thumb

Consider the Rule of 120[1], a calculation that uses your age to determine the supposedly appropriate asset allocation for your investments: The formula tells you to subtract your age from 120 to discover the percentage of equities you should hold. For many, this may make sense, given that the older you get, the lower your capacity to take on risk.

Then there is the 4% Rule. Since the mid-'90s, this has been applied universally as a rule of thumb to determine the appropriate drawdown rate and asset allocation for retirees. It suggests that if you withdraw 4% of your capital in the first year of retirement and only adjust for inflation each year thereafter – and provided that you maintain a minimum 50%

[1] This started out as the Rule of 100, but has been updated since to account for rising global life expectancy.

allocation to equities – the risk of outliving your retirement savings over a 30-year period is substantially reduced.

Another popular formula provides an estimate of the amount of time it will take an investment to double in value. The Rule of 72 suggests that by dividing 72 by the interest earned on your investment each year, expressed as a percentage, you will get a figure that represents the number of years it will take your investment to grow twofold.

Add a pinch of salt

While the rules of thumb mentioned above provide us with a starting point to guide our thinking and planning, the trouble with them, and other statements that equate averages with certainties, is that they are by nature based on assumptions and metrics applied to the average person or "typical" circumstances. The notable flaw of rules of thumb is therefore that they cannot account for every investor's unique circumstances. Averages themselves are problematic – think about the anecdote of the man who attempted to cross a river that was, on average, knee-deep, only to drown in the section that was much deeper than the average.

... rules of thumb should not be considered hard and fast instructions, but rather broad and general guidelines.

Bringing this back to investments: Consider two 35-year-old investors who are both married with two children and plan to retire at the age of 65. Thabo is the breadwinner with a stay-at-home wife. Mark has a salaried wife with parents and relatives dependent on them. While Thabo and Mark's investment horizons look the same, their profiles are clearly very different. As an investor facing greater short-term financial obligations, Mark's appetite for risk would likely be more conservative than Thabo's, given that Thabo's circumstances potentially leave him in a better position to absorb short-term market shocks.

If one applied the Rule of 120 to Mark and Thabo's profiles, both should have 85% of their portfolios invested in equities, but given Mark's responsibilities, this allocation may not be appropriate. Thabo's situation is also not without risk. As the sole breadwinner in his household, the consequences of falling ill or losing his job could have a devastating impact on his family – a factor that will also influence his risk appetite.

And what about investors who start saving for retirement late in life? A formula that de-risks your exposure to equities as you get older may not be the optimal choice. This is why, in investing, rules of thumb should always be considered with a pinch of salt.

This holds true for even the more well-known rules.

While the 4% Rule can be a good starting point for investors entering retirement, the formula may not be applicable to every investor. For instance, those who plan to delay their retirement date and work longer might not need an income for 30 years, while others may prefer to start on a higher drawdown rate and reduce their real income over time by taking below-inflation increases.

Over the past two years, we have witnessed, and many have experienced, how unexpected events or phenomena, such as the COVID-19 pandemic and the global ramifications of the Russia-Ukraine conflict, can drastically alter our financial status. For retirees, unexpected expenses could force some to deviate from the inflationary increases, and return fluctuations could mean that some may need to draw down lower income increases due to muted returns, and vice versa when strong returns are generated.

With the Rule of 72, it is impossible to predict what the future rate of return might be. A far better approach to doubling your investments would be, where possible, to increase your contributions and leverage the power of compound interest to grow your investments.

Rather than anchoring on formulae that may not be appropriate, focus on aspects of your financial plan that you can tweak and change to give you a better chance of retiring comfortably (as described below). Resources like the Allan Gray investment calculator can help you determine what your current investments could be worth in the future. It is also advisable to consult a good, independent financial adviser, who can help you devise a financial plan that takes your personal circumstances, financial obligations and personal inflation into account.

Boost your retirement savings with these pointers

Saving for retirement can feel like an insurmountable balancing act to pull off in the face of escalating living costs and the rising inflationary environment we currently find ourselves in, but fortunately, there are a few levers we can pull to help us get it right.

Beware of the lifestyle creep and plan for lifestyle inflation

As retirement savers, we face two types of inflation: the rising cost of goods and services, and lifestyle inflation, which refers to the changes in your standard of living over time as you progress in your career and your earning potential improves. Generally speaking, the more we earn, the more we spend, but it is important that we not only plan for future price increases, but also plan for future increases in our expenditure. This means upwardly adjusting your retirement saving contributions every time your salary increases.

Prioritise your retirement savings

Whenever you receive a lump sum, consider dividing the windfall between your daily and long-term needs. If you are fortunate enough to receive more than one lump sum windfall in a year, you could also make alternating contributions to the two pots. You can also supplement your retirement savings with a tax-free investment account or a unit trust. These will give you more flexibility in terms of the funds you are invested in and accessing your investments.

Decrease your expenses before retirement

Focus on paying off big-ticket assets like your home and car well before you reach retirement age, as this will significantly reduce your expenditure bill in retirement. If you can, it is advisable to start downsizing your lifestyle ahead of retirement or eliminating excessive costs and expensive debt.

Careful planning is key

As an investor, you may come across many different rules of thumb along your investment journey. These may help you make sense of how much you will need to invest to avoid outliving your retirement nest egg, but it is important not to lose sight of and account for your individual circumstances.

Thandi joined Allan Gray in 2020 as a communications specialist in the Marketing team. She holds a Bachelor of Social Science degree in Media & Writing and Politics from the University of Cape Town.

NOTES

Allan Gray Balanced and Stable Fund asset allocation as at 31 March 2022

	Balanced Fund % of portfolio			Stable Fund % of portfolio		
	Total	SA	Foreign*	Total	SA	Foreign*
Net equities	71.5	53.2	18.3	37.6	28.7	9.0
Hedged equities	6.6	1.7	4.9	10.9	2.3	8.5
Property	1.1	0.8	0.3	1.3	1.2	0.2
Commodity-linked	2.9	2.2	0.6	2.8	2.3	0.5
Bonds	13.3	10.2	3.2	34.4	28.3	6.1
Money market and bank deposits	4.5	2.2	2.3	13.0	6.9	6.1
Total	**100.0**	**70.4**	**29.6**	**100.0**	**69.6**	**30.4**

Note: There might be slight discrepancies in the totals due to rounding. *This includes African ex-SA assets.

Allan Gray Equity Fund net assets as at 31 March 2022

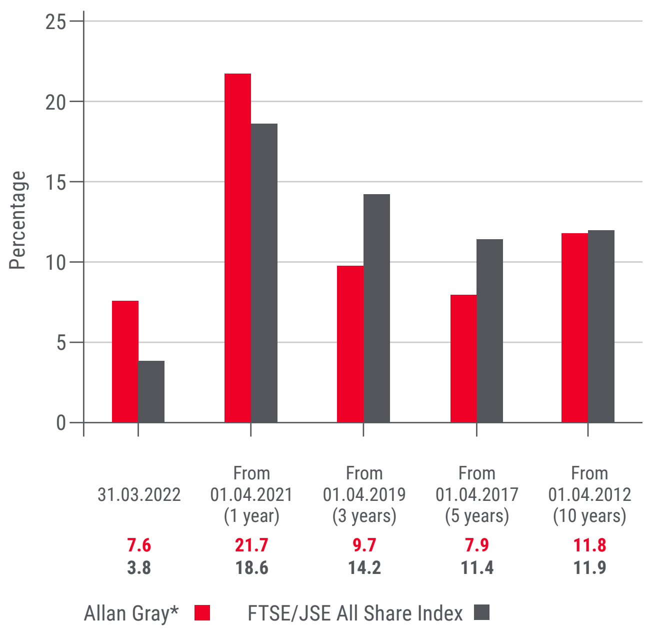
Security (Ranked by sector)	Market value (R million)	% of Fund	FTSE/JSE ALSI weight (%)
South Africa	**28 219**	**71.7**	
South African equities	**27 380**	**69.6**	
Resources	**7 886**	**20.0**	**32.1**
Glencore	2 359	6.0	
Sasol	1 174	3.0	
Sibanye-Stillwater	1 067	2.7	
Gold Fields	558	1.4	
Impala Platinum	477	1.2	
Sappi	457	1.2	
Northam Platinum	452	1.1	
AngloGold Ashanti	420	1.1	
African Rainbow Minerals	276	0.7	
Positions less than 1%[1]	645	1.6	
Financials	**8 713**	**22.1**	**25.0**
Nedbank	1 323	3.4	
Remgro	1 243	3.2	
Standard Bank	1 189	3.0	
FirstRand	803	2.0	
Reinet	755	1.9	
Old Mutual	679	1.7	
Investec	509	1.3	
Ninety One	351	0.9	
Rand Merchant Investment[2]	333	0.8	
Positions less than 1%[1]	1 528	3.9	
Industrials	**10 781**	**27.4**	**42.9**
Naspers[2]	2 043	5.2	
British American Tobacco	1 985	5.0	
Woolworths	1 284	3.3	
AB InBev	1 044	2.7	
Life Healthcare	456	1.2	
KAP Industrial	381	1.0	
MultiChoice	372	0.9	
Mondi	344	0.9	
Super Group	319	0.8	
Positions less than 1%[1]	2 552	6.5	
Commodity-linked securities	**211**	**0.5**	
Positions less than 1%[1]	211	0.5	
Bonds	**26**	**0.1**	
Positions less than 1%[1]	26	0.1	
Cash	**603**	**1.5**	
Africa ex-SA	**1 074**	**2.7**	
Equity funds	**1 074**	**2.7**	
Allan Gray Africa ex-SA Equity Fund	1 074	2.7	
Foreign ex-Africa	**10 073**	**25.6**	
Equity funds	**9 937**	**25.2**	
Orbis Global Equity Fund	4 701	11.9	
Orbis SICAV International Equity Fund[3]	3 151	8.0	
Allan Gray Frontier Markets Equity Fund Limited	1 305	3.3	
Orbis SICAV Japan Equity (Yen) Fund	425	1.1	
Orbis SICAV Emerging Markets Equity Fund	356	0.9	
Cash	**136**	**0.3**	
Totals	**39 366**	**100.0**	

[1] JSE-listed securities include equities, property and commodity-linked instruments. [2] Includes holding in stub certificates or Prosus N.V., if applicable. [3] This fund is not approved for marketing in South Africa. Reference to this fund is solely for disclosure purposes and is not intended for, nor does it constitute, solicitation for investment. **Note:** There may be slight discrepancies in the totals due to rounding. For other fund-specific information, please refer to the monthly factsheets.

Investment track record – share returns

Allan Gray Proprietary Limited global mandate share returns vs FTSE/JSE All Share Index			
Period	**Allan Gray***	**FTSE/JSE All Share Index**	**Out-/Under-performance**
1974 (from 15.6)	−0.8	−0.8	0.0
1975	23.7	−18.9	42.6
1976	2.7	−10.9	13.6
1977	38.2	20.6	17.6
1978	36.9	37.2	−0.3
1979	86.9	94.4	−7.5
1980	53.7	40.9	12.8
1981	23.2	0.8	22.4
1982	34.0	38.4	−4.4
1983	41.0	14.4	26.6
1984	10.9	9.4	1.5
1985	59.2	42.0	17.2
1986	59.5	55.9	3.6
1987	9.1	−4.3	13.4
1988	36.2	14.8	21.4
1989	58.1	55.7	2.4
1990	4.5	−5.1	9.6
1991	30.0	31.1	−1.1
1992	−13.0	−2.0	−11.0
1993	57.5	54.7	2.8
1994	40.8	22.7	18.1
1995	16.2	8.8	7.4
1996	18.1	9.4	8.7
1997	−17.4	−4.5	−12.9
1998	1.5	−10.0	11.5
1999	122.4	61.4	61.0
2000	13.2	0.0	13.2
2001	38.1	29.3	8.8
2002	25.6	−8.1	33.7
2003	29.4	16.1	13.3
2004	31.8	25.4	6.4
2005	56.5	47.3	9.2
2006	49.7	41.2	8.5
2007	17.6	19.2	−1.6
2008	−13.7	−23.2	9.5
2009	27.0	32.1	−5.1
2010	20.3	19.0	1.3
2011	9.9	2.6	7.3
2012	20.6	26.7	−6.1
2013	24.3	21.4	2.9
2014	16.2	10.9	5.3
2015	7.8	5.1	2.7
2016	12.2	2.6	9.6
2017	15.6	21.0	−5.4
2018	−8.0	−8.5	0.5
2019	6.2	12.0	−5.8
2020	−3.5	7.0	−10.5
2021	28.9	29.2	−0.3
2022 (to 31.03)	**7.6**	**3.8**	**3.8**

Returns annualised to 31.03.2022



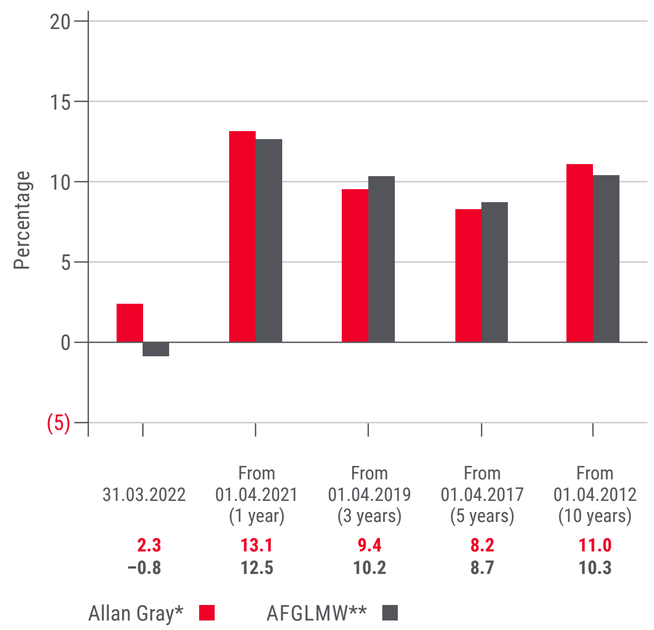
An investment of R10 000 made with Allan Gray on 15 June 1974 would have grown to R302 046 515 by 31 March 2022. By comparison, the returns generated by the FTSE/JSE All Share Index over the same period would have grown a similar investment to R14 283 070. Returns are before fees.

*Allan Gray commenced managing pension funds on 1 January 1978. The returns prior to 1 January 1978 are of individuals managed by Allan Gray, and these returns exclude income. Returns are before fees.
Note: Listed property included from 1 July 2002. Inward listed included from November 2008 to November 2011.

Investment track record – balanced returns

Allan Gray Proprietary Limited global mandate total returns vs Alexander Forbes Global Large Manager Watch			
Period	**Allan Gray***	**AFGLMW****	**Out-/Under-performance**
1974	–	–	–
1975	–	–	–
1976	–	–	–
1977	–	–	–
1978	34.5	28.0	6.5
1979	40.4	35.7	4.7
1980	36.2	15.4	20.8
1981	15.7	9.5	6.2
1982	25.3	26.2	−0.9
1983	24.1	10.6	13.5
1984	9.9	6.3	3.6
1985	38.2	28.4	9.8
1986	40.3	39.9	0.4
1987	11.9	6.6	5.3
1988	22.7	19.4	3.3
1989	39.2	38.2	1.0
1990	11.6	8.0	3.6
1991	22.8	28.3	−5.5
1992	1.2	7.6	−6.4
1993	41.9	34.3	7.6
1994	27.5	18.8	8.7
1995	18.2	16.9	1.3
1996	13.5	10.3	3.2
1997	−1.8	9.5	−11.3
1998	6.9	−1.0	7.9
1999	80.0	46.8	33.1
2000	21.7	7.6	14.1
2001	44.0	23.5	20.5
2002	13.4	−3.6	17.1
2003	21.5	17.8	3.7
2004	21.8	28.1	−6.3
2005	40.0	31.9	8.1
2006	35.6	31.7	3.9
2007	14.5	15.1	−0.6
2008	−1.1	−12.3	11.2
2009	15.6	20.3	−4.7
2010	11.7	14.5	−2.8
2011	12.6	8.8	3.8
2012	15.1	20.0	−4.9
2013	25.0	23.3	1.7
2014	10.3	10.3	0.0
2015	12.8	6.9	5.9
2016	7.5	3.7	3.8
2017	11.9	11.5	0.4
2018	−1.4	−2.1	0.7
2019	6.5	10.9	−4.4
2020	5.3	6.3	−1.0
2021	20.4	21.9	−1.5
2022 (to 31.03)	**2.3**	**−0.8**	**3.1**

Returns annualised to 31.03.2022



An investment of R10 000 made with Allan Gray on 1 January 1978 would have grown to R32 407 740 by 31 March 2022. The average total performance of global mandates of Large Managers over the same period would have grown a similar investment to R7 176 666. Returns are before fees.

*Allan Gray commenced managing pension funds on 1 January 1978. The returns prior to 1 January 1978 are of individuals managed by Allan Gray, and these returns exclude income. Returns are before fees.
**Consulting Actuaries Survey returns used up to December 1997. The return for March 2022 is an estimate. The return from 1 April 2010 is the average of the non-investable Alexander Forbes Global Large Manager Watch.
Note: Listed property included from 1 July 2002. Inward listed included from November 2008 to November 2011.

Allan Gray South African unit trusts annualised performance (rand) in percentage per annum to 31 March 2022 (net of fees)

	Assets under management (R billion)	Inception date	Since inception	10 years	5 years	3 years	1 year	Highest annual return[5]	Lowest annual return[5]
High net equity exposure (100%)									
Allan Gray Equity Fund (AGEF) Average of South African - Equity - General category (excl. Allan Gray funds)[1]	**39.4**	**01.10.1998**	**19.8** 14.7	**9.9** 10.0	**6.7** 8.1	**8.4** 11.9	**14.1** 17.8	**125.8** 73.0	**−24.3** −37.6
Allan Gray SA Equity Fund (AGDE) FTSE/JSE All Share Index including income	**4.1**	**13.03.2015**	**6.7** 8.9	**–** –	**6.8** 11.4	**9.0** 14.2	**21.1** 18.6	**57.3** 54.0	**−32.0** −18.4
Allan Gray-Orbis Global Equity Feeder Fund (AGOE) FTSE World Index	**22.9**	**01.04.2005**	**13.5** 14.1	**15.9** 18.3	**8.7** 14.6	**10.8** 15.4	**−4.4** 8.2	**78.2** 54.2	**−29.7** −32.7
Medium net equity exposure (40% - 75%)									
Allan Gray Balanced Fund (AGBF) **Allan Gray Tax-Free Balanced Fund (AGTB)** Average of South African - Multi Asset - High Equity category (excl. Allan Gray funds)[2]	**157.6** **1.9**	**01.10.1999** **01.02.2016**	**15.3** **7.5** 11.6/7.0	**9.9** **–** 9.0	**7.2** **7.1** 7.3	**8.6** **8.3** 9.1	**12.0** **11.4** 10.6	**46.1** **31.7** 41.9/30.7	**−14.2** **−13.4** −16.7/−10.3
Allan Gray-Orbis Global Balanced Feeder Fund (AGGF)[3] 60% MSCI World Index with net dividends reinvested and 40% J.P. Morgan GBI Global Index[3]	**15.1**	**03.02.2004**	**10.5** 11.0	**13.2** 14.0	**7.6** 10.2	**10.1** 9.6	**7.6** 1.8	**55.6** 38.8	**−13.7** −17.0
Low net equity exposure (0% - 40%)									
Allan Gray Stable Fund (AGSF) Daily interest rate of FirstRand Bank Limited plus 2%	**47.8**	**01.07.2000**	**11.3** 8.5	**8.5** 6.8	**7.2** 6.7	**7.1** 5.8	**10.2** 4.7	**23.3** 14.6	**−7.4** 4.6
Very low net equity exposure (0% - 20%)									
Allan Gray Optimal Fund (AGOF) Daily interest rate of FirstRand Bank Limited	**0.9**	**01.10.2002**	**7.3** 6.0	**6.2** 4.7	**3.9** 4.5	**3.2** 3.7	**13.6** 2.7	**18.1** 11.9	**−8.2** 2.5
Allan Gray-Orbis Global Optimal Fund of Funds (AGOO) Average of US$ bank deposits and euro bank deposits	**0.9**	**02.03.2010**	**6.1** 5.0	**7.0** 6.0	**1.1** 2.6	**1.5** 0.3	**4.8** −4.2	**39.6** 35.6	**−12.4** −19.1
No equity exposure									
Allan Gray Bond Fund (AGBD) FTSE/JSE All Bond Index (Total return)	**6.4**	**01.10.2004**	**9.0** 8.6	**8.4** 8.1	**9.0** 8.9	**8.0** 8.4	**11.3** 12.4	**18.0** 21.2	**−2.6** −5.6
Allan Gray Money Market Fund (AGMF) Alexander Forbes Short-Term Fixed Interest (STeFI) Composite Index[4]	**23.5**	**03.07.2001**	**7.7** 7.5	**6.4** 6.1	**6.6** 6.1	**5.7** 5.2	**4.4** 3.9	**12.8** 13.3	**4.3** 3.8

1 From inception to 28 February 2015, the benchmark was the FTSE/JSE All Share Index including income (source: IRESS).
2 From inception to 31 January 2013, the benchmark of the Allan Gray Balanced Fund was the market value-weighted average return of the funds in both the Domestic Asset Allocation Medium Equity and Domestic Asset Allocation Variable Equity sectors of the previous ASISA Fund Classification Standard, excluding the Allan Gray Balanced Fund.
3 From inception to 31 May 2021, this Fund was called the Allan Gray-Orbis Global Fund of Funds and its benchmark was 60% of the FTSE World Index and 40% of the J.P. Morgan GBI Global Index. From 1 June 2021, the Fund's investment mandate was changed from a fund of funds structure to a feeder fund structure investing solely into the Orbis SICAV Global Balanced Fund. To reflect this, the Fund was renamed and the benchmark was changed.
4 From inception to 31 March 2003, the benchmark was the Alexander Forbes 3-Month Deposit Index. From 1 April 2003 to 31 October 2011, the benchmark was the Domestic Fixed Interest Money Market Collective Investment Scheme sector excluding the Allan Gray Money Market Fund.
5 This is the highest or lowest consecutive 12-month return since inception. All rolling 12-month figures for the Fund and the benchmark are available from our Client Service Centre on request.

Allan Gray total expense ratios and transaction costs for the 3-year period ending 31 March 2022

	Fee for benchmark performance	Performance fees	Other costs excluding transaction costs	VAT	Total expense ratio	Transaction costs (incl. VAT)	Total investment charge
Allan Gray Equity Fund	1.12%	−0.56%	0.04%	0.05%	0.65%	0.10%	0.75%
Allan Gray SA Equity Fund	1.00%	−0.99%	0.01%	0.00%	0.02%	0.10%	0.12%
Allan Gray Balanced Fund	1.05%	−0.25%	0.04%	0.09%	0.93%	0.08%	1.01%
Allan Gray Tax-Free Balanced Fund	1.32%	N/A	0.04%	0.14%	1.50%	0.10%	1.60%
Allan Gray Stable Fund	1.03%	−0.17%	0.03%	0.10%	0.99%	0.06%	1.05%
Allan Gray Optimal Fund	1.00%	0.00%	0.03%	0.15%	1.18%	0.11%	1.29%
Allan Gray Bond Fund	0.28%	0.12%	0.01%	0.06%	0.47%	0.00%	0.47%
Allan Gray Money Market Fund	0.25%	N/A	0.00%	0.04%	0.29%	0.00%	0.29%
Allan Gray-Orbis Global Equity Feeder Fund	1.49%	−0.65%	0.05%	0.00%	0.89%	0.09%	0.98%
Allan Gray-Orbis Global Balanced Feeder Fund	1.46%	−0.54%	0.06%	0.00%	0.98%	0.08%	1.06%
Allan Gray-Orbis Global Optimal Fund of Funds	1.00%	−0.01%	0.09%	0.00%	1.08%	0.13%	1.21%

The total expense ratio (TER) is the annualised percentage of the Fund's average assets under management that has been used to pay the Fund's actual expenses over the past three years. The TER includes the annual management fees that have been charged (both the fee at benchmark and any performance component charged), VAT and other expenses like audit and trustee fees. Transaction costs (including brokerage, securities transfer tax, Share Transactions Totally Electronic (STRATE) and FSCA Investor Protection Levy and VAT thereon) are shown separately. Transaction costs are necessary costs in administering the Fund and impact Fund returns. They should not be considered in isolation as returns may be impacted by many other factors over time, including market returns, the type of financial product, the investment decisions of the investment manager, and the TER. Since Fund returns are quoted after the deduction of these expenses, the TER and transaction costs should not be deducted again from published returns. As unit trust expenses vary, the current TER cannot be used as an indication of future TERs. A higher TER does not necessarily imply a poor return, nor does a low TER imply a good return. Instead, when investing, the investment objective of the Fund should be aligned with the investor's objective and compared against the performance of the Fund. The TER and other funds' TERs should then be used to evaluate whether the Fund performance offers value for money. The sum of the TER and transaction costs is shown as the total investment charge (TIC).

Foreign domiciled funds annualised performance (rand) in percentage per annum to 31 March 2022 (net of fees)

	Inception date	Since inception	10 years	5 years	3 years	1 year	Highest annual return[5]	Lowest annual return[5]
High net equity exposure								
Orbis Global Equity Fund	**01.01.1990**	**17.2**	**15.9**	**8.6**	**10.6**	**−4.5**	**87.6**	**−47.5**
FTSE World Index		13.7	18.4	14.6	15.5	8.4	54.2	−46.2
Orbis SICAV Japan Equity (Yen) Fund	**01.01.1998**	**13.6**	**14.2**	**7.3**	**7.2**	**−6.8**	**94.9**	**−40.1**
Tokyo Stock Price Index		9.0	13.8	7.5	6.3	−8.5	91.0	−46.4
Orbis SICAV Emerging Markets Equity Fund (US$)[6]	**01.01.2006**	**12.1**	**10.9**	**3.4**	**3.1**	**−13.6**	**58.6**	**−34.2**
MSCI Emerging Markets Equity (Net) (US$)[6]		12.4	12.2	7.8	5.2	−12.4	60.1	−39.7
Allan Gray Africa ex-SA Equity Fund (C class)	**01.01.2012**	**12.0**	**11.1**	**13.7**	**7.5**	**14.1**	**65.6**	**−24.3**
Standard Bank Africa Total Return Index		8.1	7.5	13.2	15.3	20.6	41.4	−29.4
Allan Gray Australia Equity Fund	**04.05.2006**	**14.6**	**15.2**	**10.8**	**12.4**	**18.6**	**99.5**	**−55.4**
S&P/ASX 300 Accumulation Index		12.7	13.7	10.9	13.3	12.3	55.6	−45.1
Allan Gray Frontier Markets Equity Fund (C class)	**03.04.2017**	**6.1**	**–**	**–**	**4.3**	**1.6**	**26.4**	**−11.0**
MSCI Frontier Emerging Markets Index		5.1	–	–	2.4	10.3	15.9	−12.0
Medium net equity exposure								
Orbis SICAV Global Balanced Fund	**01.01.2013**	**13.7**	**–**	**7.9**	**10.3**	**8.0**	**54.4**	**−9.8**
60% MSCI World Index with net dividends reinvested and 40% J.P. Morgan GBI Global Index		13.5	–	10.1	9.5	1.9	40.2	−8.4
Allan Gray Australia Balanced Fund	**01.03.2017**	**9.8**	**–**	**9.1**	**10.8**	**9.9**	**29.1**	**−5.3**
The custom benchmark comprises the S&P/ASX 300 Accumulation Index (36%), S&P/ASX Australian Government Bond Index (24%), MSCI World Index (net dividends reinvested) expressed in AUD (24%) and J.P. Morgan GBI Global Index expressed in AUD (16%).		9.6	–	8.9	9.3	3.0	25.1	−5.8
Low net equity exposure								
Allan Gray Australia Stable Fund	**01.07.2011**	**10.4**	**9.6**	**6.2**	**7.4**	**4.0**	**32.7**	**−8.9**
Reserve Bank of Australia cash rate		5.9	4.9	2.3	2.6	−2.4	28.8	−15.5
Very low net equity exposure								
Orbis Optimal SA Fund (US$)	**01.01.2005**	**8.6**	**8.4**	**1.9**	**2.9**	**8.0**	**48.6**	**−15.7**
US$ Bank deposits		7.3	7.5	3.0	1.2	−0.9	57.9	−25.6
Orbis Optimal SA Fund (Euro)	**01.01.2005**	**6.4**	**5.5**	**0.8**	**1.1**	**1.9**	**44.1**	**−19.3**
Euro Bank deposits		5.2	4.5	2.0	−0.5	−6.9	40.2	−20.9
No equity exposure								
Allan Gray Africa Bond Fund (C class)[7]	**27.03.2013**	**12.4**	**–**	**10.0**	**5.9**	**1.8**	**28.9**	**−7.4**
FTSE 3-Month US T Bill + 4% Index[7]		5.9	–	6.2	6.3	2.8	24.7	−12.3

Performance as calculated by Allan Gray

[5] This is the highest or lowest consecutive 12-month return since inception. All rolling 12-month figures for the Fund and the benchmark are available from our Client Service Centre on request.

[6] From inception to 31 October 2016, this Fund was called the Orbis SICAV Asia ex-Japan Equity Fund and its benchmark was the MSCI Asia ex-Japan Index. From 1 November 2016, the Fund's investment mandate was broadened to include all emerging markets. To reflect this, the Fund was renamed and the benchmark was changed.

[7] From inception to 31 December 2020, this Fund was called the Allan Gray Africa ex-SA Bond Fund and its benchmark was the J.P. Morgan GBI-EM Global Diversified Index. From 1 January 2021, the Fund's investment mandate was broadened to include South African investments. To reflect this, the Fund was renamed and the benchmark was changed.

IMPORTANT INFORMATION FOR INVESTORS

Information and content

The information in and content of this publication are provided by Allan Gray as general information about the company and its products and services. ("Allan Gray" means Allan Gray Proprietary Limited and all of its subsidiaries and associate companies, and "the company" includes all of those entities.) Allan Gray does not guarantee the suitability or potential value of any information or particular investment source. The information provided is not intended to, nor does it constitute financial, tax, legal, investment or other advice. Before making any decision or taking any action regarding your finances, you should consult a qualified financial adviser. Nothing contained in this publication constitutes a solicitation, recommendation, endorsement or offer by Allan Gray; it is merely an invitation to do business.

Allan Gray has taken and will continue to take care that all information provided, in so far as this is under its control, is true and correct. However, Allan Gray shall not be responsible for and therefore disclaims any liability for any loss, liability, damage (whether direct or consequential) or expense of any nature whatsoever which may be suffered as a result of or which may be attributable, directly or indirectly, to the use of or reliance on any information provided.

Allan Gray Unit Trust Management (RF) (Pty) Ltd (the "Management Company") is registered as a management company under the Collective Investment Schemes Control Act 45 of 2002, in terms of which it operates unit trust portfolios under the Allan Gray Unit Trust Scheme, and is supervised by the Financial Sector Conduct Authority (FSCA). Allan Gray (Pty) Ltd (the "Investment Manager"), an authorised financial services provider, is the appointed investment manager of the Management Company and is a member of the Association for Savings & Investment South Africa (ASISA). Collective investment schemes in securities (unit trusts or funds) are generally medium- to long-term investments. Except for the Allan Gray Money Market Fund, where the Investment Manager aims to maintain a constant unit price, the value of units may go down as well as up.

Past performance is not necessarily a guide to future performance. The Management Company does not provide any guarantee regarding the capital or the performance of its funds. Funds may be closed to new investments at any time in order to be managed according to their mandates. Unit trusts are traded at ruling prices and can engage in borrowing and scrip lending.

Performance

Performance figures are provided by the Investment Manager and are for lump sum investments with income distributions reinvested. Where annualised performance is mentioned, this refers to the average return per year over the period. Actual investor performance may differ as a result of the investment date, the date of reinvestment and applicable taxes. Movements in exchange rates may also cause the value of underlying international investments to go up or down. Certain unit trusts have more than one class of units and these are subject to different fees and charges. Unit trust prices are calculated on a net asset value basis, which is the total market value of all assets in the fund, including any income accruals and less any permissible deductions from the fund, divided by the number of units in issue. Forward pricing is used and fund valuations take place at approximately 16:00 each business day. Purchase and redemption requests must be received by the Management Company by 11:00 each business day for the Allan Gray Money Market Fund, and by 14:00 each business day for any other Allan Gray unit trust to receive that day's price. Unit trust prices are available daily on www.allangray.co.za. Permissible deductions may include management fees, brokerage, securities transfer tax, auditor's fees, bank charges and trustee fees. A schedule of fees, charges and maximum commissions is available on request from Allan Gray.

Benchmarks

FTSE/JSE All Share Index, FTSE/JSE Capped Shareholder Weighted All Share Index and FTSE/JSE All Bond Index

The FTSE/JSE All Share Index, FTSE/JSE Capped Shareholder Weighted All Share Index, and FTSE/JSE All Bond Index (the FTSE/JSE indices) are calculated by FTSE International Limited ("FTSE") in conjunction with the JSE Limited ("JSE") in accordance with standard criteria. The FTSE/JSE indices are the proprietary information of FTSE and the JSE. All copyright subsisting in the FTSE/JSE indices' values and constituent lists vests in FTSE and the JSE jointly. All their rights are reserved.

FTSE Russell Index

Source: London Stock Exchange Group plc and its group undertakings (collectively, the "LSE Group"). © LSE Group 2022. FTSE Russell is a trading name of certain of the LSE Group companies. "FTSE®" "Russell®", "FTSE Russell®", is/are a trade mark(s) of the relevant LSE Group companies and is/are used by any other LSE Group company under license. All rights in the FTSE Russell indexes or data vest in the relevant LSE Group company which owns the index or the data. Neither LSE Group nor its licensors accept any liability for any errors or omissions in the indexes or data and no party may rely on any indexes or data contained in this communication. No further distribution of data from the LSE Group is permitted without the relevant LSE Group company's express written consent. The LSE Group does not promote, sponsor or endorse the content of this communication.

J.P. Morgan Index

Information has been obtained from sources believed to be reliable but J.P. Morgan does not warrant its completeness or accuracy. The Index is used with permission. The Index may not be copied, used, or distributed without J.P. Morgan's prior written approval. Copyright 2022, J.P. Morgan Chase & Co. All rights reserved.

MSCI Index

Source: MSCI. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indexes or any securities or financial products. This report is not approved, endorsed, reviewed or produced by MSCI. None of the MSCI data is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such.

Understanding the funds

Investors must make sure that they understand the nature of their choice of funds and that their investment objectives are aligned with those of the fund(s) they select. The Allan Gray Equity, Balanced, Stable and rand-denominated offshore funds may invest in foreign funds managed by Orbis Investment Management Limited, our offshore investment partner.

A feeder fund is a unit trust that invests in another single unit trust, which charges its own fees. A fund of funds is a unit trust that invests in other unit trusts, which charge their own fees. Allan Gray does not charge any additional fees in its feeder funds or funds of funds.

The Allan Gray Money Market Fund is not a bank deposit account. The Fund aims to maintain a constant price of 100 cents per unit. The total return an investor receives is made up of interest received and any gain or loss made on instruments held by the Fund. While capital losses are unlikely, they can occur if, for example, one of the issuers of an instrument defaults. In this event, investors may lose some of their capital. To maintain a constant price of 100 cents per unit, investors' unit holdings will be reduced to the extent of such losses. The yield is calculated according to applicable ASISA standards. Excessive withdrawals from the Fund may place it under liquidity pressure; if this happens, withdrawals may be ring-fenced and managed over a period of time.

Additional information for retirement fund members and investors in the tax-free investment account, living annuity and endowment

The Allan Gray Retirement Annuity Fund, Allan Gray Pension Preservation Fund, Allan Gray Provident Preservation Fund and Allan Gray Umbrella Retirement Fund (comprising the Allan Gray Umbrella Pension Fund and Allan Gray Umbrella Provident Fund) are all administered by Allan Gray Investment Services (Pty) Ltd, an authorised administrative financial services provider and approved pension funds administrator under section 13B of the Pension Funds Act 24 of 1956. Allan Gray (Pty) Ltd, also an authorised financial services provider, is the sponsor of the Allan Gray retirement funds. The Allan Gray Tax-Free

Investment Account, Allan Gray Living Annuity and Allan Gray Endowment are administered by Allan Gray Investment Services (Pty) Ltd, an authorised administrative financial services provider, and underwritten by Allan Gray Life Ltd, an insurer licensed to conduct investment-linked life insurance business as defined in the Insurance Act 18 of 2017. The underlying investment options of the Allan Gray individual life and retirement products are portfolios of collective investment schemes in securities (unit trusts or funds) and life-pooled investments.

Tax note

In accordance with section 11(i) of the Botswana Income Tax Act (Chapter 52;01), an amount accrued to any person shall be deemed to have accrued from a source situated in Botswana where it has accrued to such person in respect of any investment made outside Botswana by a resident of Botswana, provided that section 11(i) shall not apply to foreign investment income of non-citizens resident in Botswana. Botswana residents who have invested in the shares of the Fund are therefore requested to declare income earned from this Fund when preparing their annual tax returns. The Facilities Agent for the Fund in Botswana is Allan Gray Botswana (Pty) Ltd at 2nd Floor, Building 2, Central Square, New CBD, Gaborone, where investors can obtain a prospectus and financial reports.

About the paper

The Allan Gray Quarterly Commentary is printed on paper made from trees grown specifically for paper manufacturing. The paper is certified by the Forest Stewardship Council (FSC), an organisation which promotes responsible management of the world's forests.

Registration number
2005/002576/07

Business address
1 Silo Square
V&A Waterfront
Cape Town
8001

P O Box 51318
V&A Waterfront
Cape Town
8002
South Africa

Client Service Centre
T 0860 000 654 or +27 (0)21 415 2301
F 0860 000 655 or +27 (0)21 415 2492
E info@allangray.co.za
www.allangray.co.za


ALLANGRAY