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NEDGROUP INVESTMENTS ENTREPRENEUR FUND

Quarter Two, 2023





Nedgroup Investments Entrepreneur Fund

Performance to 30 June 2023	Nedgroup Investments Entrepreneur Fund ¹	ASISA category average	Small Cap Index	Mid Cap Index
3 months	-2.0%	-0.9%	0.5%	-0.2%
12 months	4.2%	5.7%	10.8%	7.5%

Market commentary

It has been a gruelling first half of the year with domestic economic activity negatively impacted by higher levels of loadshedding, political uncertainty, sticky inflation and a steeper rise in interest rates than forecast at the beginning of the year. As a result of these factors, GDP growth expectations continue to be revised lower (no growth expected for the 2023 calendar year). In addition, the market remains concerned with the South African government's stance on the Russia/Ukraine conflict, which has added to SA's country risk premium, with bond yields rising and the rand vulnerable.

South Africa has adopted what it says is a non-aligned stance toward the war in Ukraine and it has abstained from several United Nations votes condemning Russia's actions. Its neutrality was called into question in May, when US Ambassador Reuben Brigety accused South Africa of supplying weapons to Russia. While President Cyril Ramaphosa denied the allegation, this event triggered a substantial sell-off in South African assets and the rand fell to a record low against the US\$ given the risk of potential sanctions by the USA or other Western Allies. Although sanctions are unlikely at this stage, this could exert a devastating effect on an economy that is already fragile because of long-standing political mismanagement.

As a consequence of the abovementioned issues, investor perceptions and business confidence remain constrained with several business leaders warning that South Africa risks becoming a failed state unless its myriad of problems are addressed. These worries are also evident amongst SA consumers, with the latest FNB/BER Consumer Confidence Index for Q2 measuring -25, the second-lowest reading since 1994.

Toward the end of Q2 there has been some relief from these issues - the severity of load shedding has diminished, Operation Vulindlela continues to spur structural change in key areas, President Cyril Ramaphosa was cleared in the final Phala Phala investigation and the ANC have been jolted into emphasising the country's professed non-alignment in the Russia/Ukraine conflict. These developments have reduced underlying anxiety to some of the most pressing investor concerns that have characterised sentiment towards SA for much of this year. As welcome as this is, it is uncertain how durable this reprieve will prove to be.

Despite the above-mentioned issues, SA equities have outperformed other domestic asset classes year-to-date with a total return of +5.9%.

In contrast, it has been a strong first half of the year for global markets (notably in the US and Europe) despite slowing economic conditions, hawkish central bank rhetoric and ongoing geopolitical tensions. Year-to-date, MSCI All World Index has returned +13.9% in US\$, the S&P500 is only 8% off its all-time high, and the European region gained +14.2%. The MSCI Emerging Market Index has posted a more modest return of +5.1% (+10.1%

¹ Net return for the Nedgroup Investments Entrepreneur Fund, A class. Source: Morningstar (monthly data series).





excluding China). Chinese equities have sold off as investors question the pace and sustainability of the post Covid rebound.

The US market was driven by the return of 'Growth' outperformance and a generative artificial intelligence (AI) fuelled boom which helped the Nasdaq rally +39% in the first half – this is the strongest first six months of the year on record. Nvidia soared to a \$1 trillion valuation on the frenzied AI narrative and Apple made Wall Street history by becoming the first company to exceed a \$3 trillion valuation. Of concern, the concentration of returns has been very narrow; mostly driven by a handful of technology stocks with only 32% of US stocks outperforming the market year-to-date, the lowest first half breadth on record for US equities.

Looking ahead, we should not confuse the narrow market rally with the health of the global economy. Core inflation measures in developed markets remain stubbornly high, with US rate cuts only expected in 2024 (much later than what was expected at the beginning of the year). Higher borrowing costs will continue to test economic resilience and geopolitics will add to unpredictable economic outcomes. Investors should be prepared for further market volatility.

Portfolio Commentary

In Q2 2023, the JSE All Share Index (ALSI) posted a total return of +0.7%. The Midcap Index returned -0.2% and the Smallcap Index, +0.5%. Within equities, SA Financials returned +5.3% and SA Industrials returned +3.4%. SA Resources lost -6.1%, with the largest losses coming from Industrial Materials (-14.8%), Oil, Gas & Coal (-7.5%) and Precious Metals (-7.0%). The Rand lost another 5.9% against the USD (10.6% for the first half of 2023), ending the quarter at 18.84 to the US\$.

Four of the top five contributors are core holdings in the fund that we regard as best-in-class in their respective industries and remain attractively priced. PSG Konsult (in the process of changing its name to PSG Financial Services), is a diversified financial holding company (Wealth, Asset Management, Insurance) with solid brands and impressive technology. CMH, distributes a number of well-known vehicles in addition to having a solid car rental operation (First Car Rental). The company is attractively priced (4.5x PE, >10% dividend yield), has a solid balance sheet and attractive operating metrics (return on shareholder funds = 37%). Adcock Ingram is widely known for brands like Panado and Allergex, has managed to grow earnings despite the SA macro environment, and has bought back about 5% of its shares over the past year. Investors will be familiar with our ADVTECH holding, which has done well for the fund over recent years. Given the current state of the public schooling system, plus limited prospects of sustainable improvement, the private education space is likely to increase in relevance. Curro is also a beneficiary of this theme and we have used the recent share price weakness to establish a position in the company given the now reasonable valuation.

Despite being a relatively small position in the fund, Transaction capital was once again a top detractor to performance. The company has made certain leadership changes in SA Taxi and Nutun, as well as bolstering the Gomo offering by introducing an operational and funding partner into the business, which should facilitate more transactions in SA Taxi and WeBuyCars. The biggest uncertainty remains funding arrangements in SA Taxi. Sun International took a breather in Q2, after a strong Q1 performance. The company continues to enjoy a recovery in activity, with tourism still to recover to pre-covid levels. South Africa continues to be a desirable destination for most international travellers, as recently shown by a survey in the UK noting Cape Town as the most preferred travel destination in the World. KAP, as a manufacturer, has been severely affected by loadshedding, as illustrated by the weak operational update released in the quarter. Finally, our holding in





Impala was negatively impacted by falling commodity prices. The PGM basket price continued the declining trend observed in the first quarter, partially softened by a weak rand. The Rhodium price, having traded above \$20,000 an ounce just over a year ago, declined to a low of \$6,000 during the quarter (with the price dipping below \$4,000 post quarter-end). Overall the fund has negligible exposure to the Basic Materials sector.

Top contributors	Average weight	Performance contribution	Top detractors	Average weight	Performance contribution
PSG Konsult	3.9%	0.5%	Transaction Capital	1.6%	-1.2%
Combined Motor Holdings	4.8%	0.4%	Sun International	2.0%	-1.1%
Adcock Ingram	3.2%	0.3%	KAP	2.0%	-0.6%
Curro	0.9%	0.3%	Impala Platinum	2.4%	-0.5%
ADvTECH	4.7%	0.2%	Kaap Agri	3.0%	-0.3%
Total		1.7%	Total		-3.7%

Current positioning and outlook

Small and midcap companies, being mainly domestic companies, are closely tied to the South African macro-economic environment. As such, the low business and consumer confidence, weak ZAR, possibility of sanctions and lack of electricity is very challenging for these companies. Thankfully, post the “peak pessimism” we saw earlier in the quarter, the government appears galvanised to turn things around. An improvement from the low base should provide a reprieve for these companies, whose management teams are adept at operating under harsh conditions.

At the risk of sounding like a broken record, our approach and positioning has not changed, compared to the previous quarter. We still like strong, quality companies who have found a way, either through market share growth or innovation, to eke out growth in this weak environment. Since the sector is out of favour given the number of challenges, are able to own and seek out quality companies at very attractive valuation, as illustrated by the portfolio trading at an attractive PE of 8.1x and supportive dividend yield of 5.6%. As we have seen in the past, alternative buyers are always on the lookout for attractively priced quality companies, and we expect this to be the case if valuations remain where they are.

Responsible Investment

We focus on doing the right thing for our clients, community and the environment and we expect the same from the companies in which we invest. We seek to invest in companies that are well positioned to provide sustainable returns into the future and that consider their impact on all stakeholders. In our analysis, we focus on business issues we believe to be material to long-term stakeholder interests. We view financial metrics and factors classified as environmental, social and governance (“ESG”) as intertwined, and essential for a comprehensive understanding of the business and its financial strength.

Abax actively and consistently engages with companies and other stakeholders to address ESG issues. Notable engagements relevant to the fund during the first quarter of 2023 include:

- EWT Business of Biodiversity Conference: Participated in various sessions of facilitated debate of business response and incorporation of environmental impact across their activities and engagement thereon.





- Nedgroup Investments Biodiversity Workshop: Participated in an industry workshop providing context to global and local Biodiversity risks and opportunities, and importantly what practical steps can be implemented.

Conclusion

Expectations are now that inflation and interest rates will be higher for longer and that economic growth will come under increasing strain in the second half of the year. The South African equity market remains very attractively priced, but the outlook fragile given lower commodity prices, a deteriorating fiscal position, ongoing energy uncertainty and falling growth forecasts. The pre 2024 election populist push is also starting to gather momentum (namely the NHI Bill) and could also frustrate economic outcomes and equity market performance.

There are reasons for caution, but this market is well suited to our investment approach, and we will use market uncertainty / volatility to our advantage. As the economic outlook comes under increasing pressure, we believe that our diversified holdings in quality companies should stand investors in good stead - the attributes of earnings resilience and strong balance sheets have enabled quality companies to survive multiple economic cycles with their market position and economics intact, while delivering returns to shareholders.

We are confident in our portfolio holdings' long-term prospects and remain focused on finding companies with competitive advantages that we believe can compound earnings and cash flows over the long term. The fund trades on a PE of 8.1x and offers a dividend yield of 5.6%.





Disclaimer

WHO WE ARE

Nedgroup Collective Investments (RF) Proprietary Limited is an authorised Collective Investment Scheme and the representative of Nedgroup Investments Funds PLC in terms of the Collective Investment Schemes Control Act. It is a member of the Association of Savings & Investment South Africa (ASISA)..

OUR TRUSTEE

The Standard Bank of South Africa Limited is the registered trustee.
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HOW ARE OUR FUNDS PRICED

Funds are valued daily at 15:00. Instructions must reach us before 14:00 (12:00 for Nedgroup Money Market Fund) to ensure same day value. Prices are published daily on our website and in selected major newspapers.

FEES

A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

DISCLAIMER

Unit trusts are generally medium to long-term investments. The value of your investment may go down as well as up. Past performance is not necessarily a guide to future performance. Nedgroup Investments does not guarantee the performance of your investment and even if forecasts about the expected future performance are included you will carry the investment and market risk, which includes the possibility of losing capital. Our funds are traded at ruling prices and can engage in borrowing and scrip lending.

Some funds may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks, which could include foreign exchange risks, market conditions and macro-economic and political conditions.

A fund of funds may only invest in other funds, and a feeder fund may only invest in another single fund, both will have funds that levy their own charges, which could result in a higher fee structure.

The Nedgroup Investments Money Market Fund offering aims to maintain a constant price of 100 cents per unit. A money market fund is not a bank deposit. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument held. In most cases the return will merely have the effect of increasing or decreasing the daily yield, but in an extreme case it can have the effect of a capital loss. Excessive withdrawals from the fund may place the fund under liquidity pressures and that in such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. The yield is calculated using an annualised seven day rolling average as at the relevant dates provided for in the fund fact sheet. Nedgroup Investments has the right to close its funds to new investors in order to manage it more efficiently.

NEDGROUP INVESTMENTS CONTACT DETAILS

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