Robert Cowen Investments

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Newsletter

end March 2019

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The Family Office

You are welcome to pass this newsletter on to friends who may wish to learn more about investment.
To be added to our email, contact alan@rcinv.co.za

"The greatest reward for doing is the opportunity to do more."
~ *Vince Lombardi*

"Being busy is a form of laziness – lazy thinking and indiscriminate action."
~ *Tim Ferris*

Visit our website: www.rcinv.co.za for back copies of the newsletter, background information, etc.

RCI BCI Flexible Fund closed March at 355.18c, up 1.6% for the month and 4.83% over 12 months.

RCI BCI Worldwide Flex closed March at 119.33c, up 4.32% for the month and 23.8% over 12 months.

What do we have to say this month? The interesting thing to point out is that our overseas portfolios are flying in both rand and dollar terms. Our unit trust which specialises in offshore shares, RCI BCI World Wide Flexible is up 4.32% for the month, 10.92% for the year and 23.8% over 12 months when measured in rands. No wonder we say: "Live local but Invest Global!"

By comparison, everything else is boring. SA's largest export is iron ore and the article on page 2 shows it has just gone to a recent high.

We put in **Anchor's views of local and overseas markets.**

Mike Gresty then explains how Naspers, South Africa's (and generally your) biggest holding **is going to split** in the next few months in an attempt to increase long-term value.

Will, Estates and the process that follows – what happens when someone close to you dies? DI Haiden has written an article on the subject. Let us know if you want to discuss your personal circumstances.

The world is better than a century ago: Two great graphs from Adrian Gore, the boss of Discovery.

Ignore the Brexit Scare stories.

In our conclusion we comment on South Africa postponing its downgrade and why we think we have seen the bottom in the South African market for the next while.

The strong demand for South Africa's commodities comes from unprecedented urbanization in China

The scale and pace of China's urbanization continues at an unprecedented rate. If current trends hold, China's urban population will hit the one billion mark by 2030. In 20 years, China's cities will have added 350 million people more than the entire population of the United States today. By 2025, China will have 221 cities with one million-plus inhabitants – compared with 35 cities of this size in Europe today – and 23 cities with more than five million. For companies in China and around the world, the scale of China's urbanization promises substantial new markets and investment opportunities.

McKinsey and Company, Feb 2019, Jonathon Woetzel et al.

What is happening in South Africa and the world, in terms of investments? The Anchor view:

Local Market Commentary – March 2019

South Africans will probably remember March mostly for the 10 consecutive days of power cuts implemented by Eskom, pessimism peaked halfway through that period when Public Enterprises Minister, Pravin Gordhan, suggested that staff were still getting to the bottom of the issues Eskom was facing and how long it would take to resolve them. Stocks most exposed to South African consumers bore the brunt of this pessimism. Banks were among the worst performers, (ABSA and Nedbank were down 16% and 12%, respectively), while retailer Mr Price declined by 12%.

https://anchorcapital.co.za/article/?local-market-commentary-march-2019 to read the full article.

Global Market Commentary – March 2019

Central banks were in the spotlight in March, with the European Central Bank (ECB) and the US Federal Reserve (Fed) holding meetings during the month. As German exports showed the worst slump in six years, the ECB pledged more cheap funding for banks and pushed out its expectation for rate hikes from this year to the next and took a knife to the region's 2019 growth forecast (cutting it to 1.1% from 1.7%). Later in March, the Fed also struck a dovish tone.

https://anchorcapital.co.za/article/?global-market-commentary-march-2019 to read the full article.

Mike Gresty's thoughts on Naspers' decision to split its share

Naspers' Euronext listing plan – a sting in the tail for retail investors?

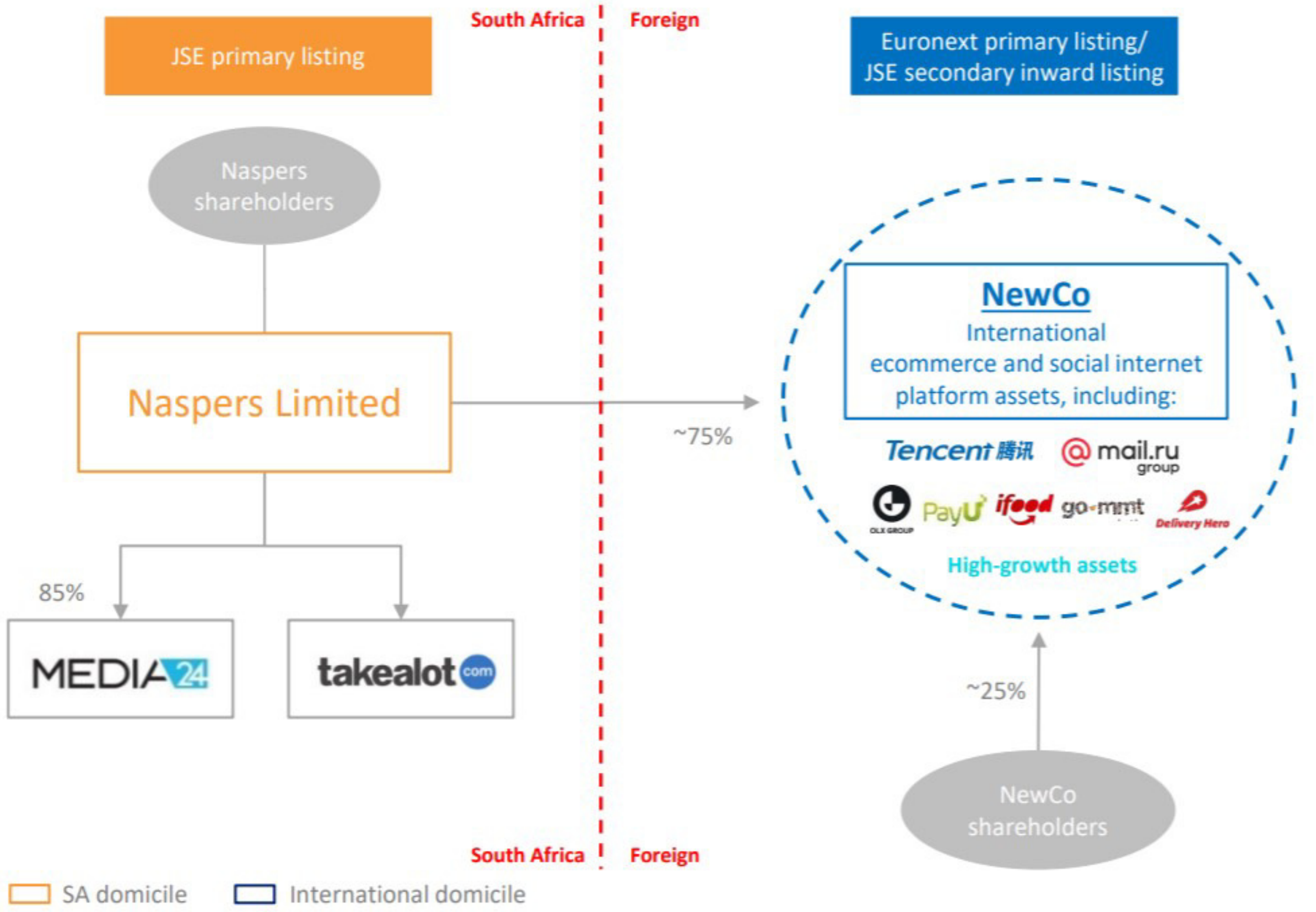
At the end of March, Naspers announced that it plans to list a company (called NewCo for now) on the Euronext Exchange in Amsterdam which will hold all of Naspers's non-South African investments. We will have to wait for the prospectus to confirm the details but, in the meantime, we provide our thoughts on how Naspers' plan might play out for you.

Naspers will make a "capitalisation award" to its shareholders of an instrument that shareholders can elect to exchange either for shares in NewCo or for more shares in Naspers. While Naspers hopes that this will narrow the discount at which the group trades to the value of its net assets, we think it will lead to a potentially unappealing choice for tax-sensitive retail investors. Electing to take up shares in NewCo will trigger a capital gain. Alternatively, electing to take up further Naspers shares avoids triggering a capital gain, but investors may find this vehicle trades at a larger discount than it did before.

What will the Naspers structure look like once this transaction is complete?

Naspers anticipates that, once the transaction is complete, around 25% of NewCo will be owned directly by its shareholders, leaving Naspers with a 75% stake in NewCo, as well as its South African assets (immaterial). The new structure is explained in Figure 1 below.

Figure 1: Naspers structure following proposed transaction



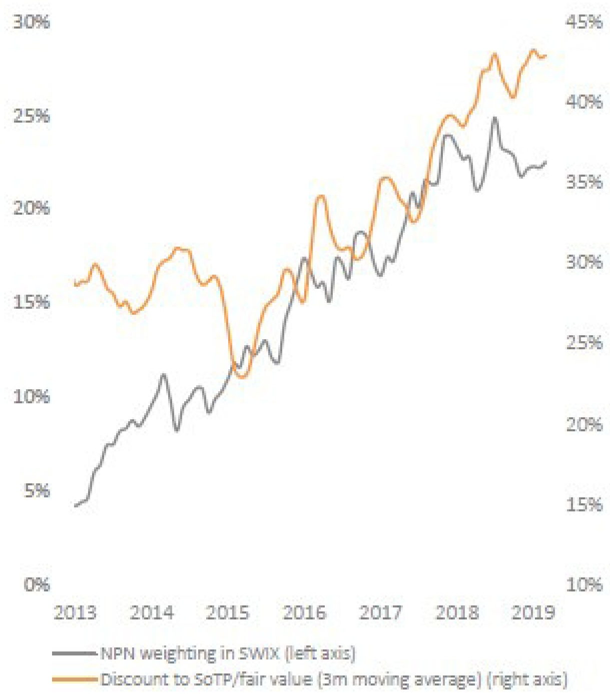
Source: Company presentation

As far as timing is concerned, at this stage, Naspers has said that it will take place no sooner than the second half of 2019.

Why is Naspers doing this?

Naspers hopes that the listing of NewCo on the Euronext exchange will be a step towards narrowing the discount at which it trades, relative to its net asset value. In the South African equity market there are few topics that have been debated more extensively than the reasons for, and likely direction of, the Naspers discount. This discount has widened in recent years and one of the important contributory factors believed to be responsible is that its outperformance of the rest of the market (thanks largely to the stellar performance of its main asset – Tencent) has led to it becoming too large for the SA market. As Figure 2 below shows, since 2013 its weighting in the JSE All Share SWIX Index has risen from just 5% to >20%. As the size of Naspers has grown, it has increasingly bumped up against the single stock concentration risk limits of institutional funds, making them forced sellers as the share continues to rise. Certainly, Figure 2 suggests this has at least been a contributory factor to the widening discount.

Figure 2: The size of Naspers on the JSE All Share SWIX



Source: Bloomberg

By listing NewCo on Euronext where: (1) its size will not be a constraint; (2) it will be eligible for inclusion in more indices, thus attracting passive index-linked buyers; and (3) developed market funds that could not buy Naspers/ Tencent before, due to limitations on their mandate, will be able to invest for the first time. NewCo, it is hoped, will trade at a lower discount to its net asset value than Naspers has done historically.

So, will Naspers' plan work?

Eliminating the size constraint and opening up NewCo to new pools of capital that had not previously had the opportunity to invest is certainly a compelling argument as to why NewCo will trade at a smaller discount to its net asset value than has been the case for Naspers. However, what is less clear is what happens to the discount in Naspers itself after the creation of NewCo. Although, admittedly, Figure 2 above reveals the discount is already extremely large and close to its historic high, we think there are a number of reasons the discount in Naspers may actually widen further post the creation of NewCo:

- The creation of NewCo introduces a new investment holding company between Naspers and the underlying investments. This introduces the possibility of a double holding company discount being applied by investors.
- Shifting 25% of Naspers's market capitalisation into NewCo will not reduce its size by enough to prevent it from hitting concentration limits in SA. Many funds may continue to see Naspers and NewCo as a single entity anyway since they are essentially exposed to the same assets.
- Institutions that do not trigger a capital gain by trading may seek to switch out of Naspers and into NewCo post the listing of NewCo, placing further selling pressure on Naspers.
- A possible lack of appeal of South African assets that remain in Naspers (albeit not very material) and value leakage resulting from existing long-term management incentives linked to Naspers shares.

Only time will tell how Mr. Market decides to treat the discounts in Naspers and NewCo. However, the fact that Naspers soon reversed the initial rally in its share price on release of the announcement could be interpreted to mean that the market anticipates a smaller discount on NewCo and a slightly wider discount on Naspers equals no material change in the overall discount from before!

The Hobson's choice facing retail investors

If the market's response so far suggests Naspers' creation of NewCo is much ado about nothing, it is important to realise this does not necessarily apply to retail investors who hold Naspers directly. As such, for retail investors who hold Naspers shares in a tax-sensitive form, we think they will face the choice to either:

1. opt to exchange the instruments that Naspers issues for NewCo shares and, in so doing, trigger a capital gain on around 25% of their Naspers investment; or

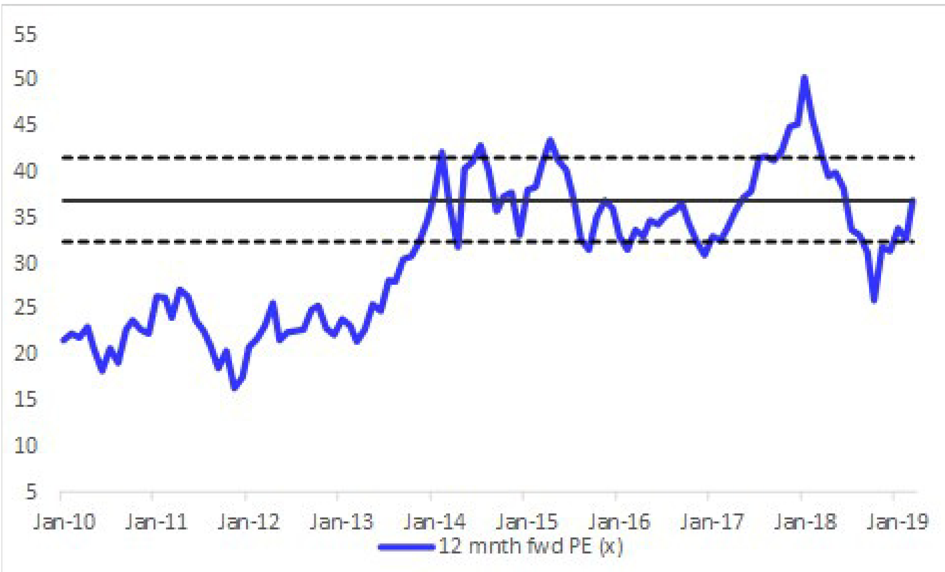
2. opt to exchange the instruments that Naspers issues for more Naspers shares. This will avoid triggering a capital gain but runs the risk that the value of their Naspers investment falls because Mr. Market begins to apply a larger discount to Naspers for the reasons discussed above.

Is there anything that can be done to avoid facing this Hobson's choice?

For investors that have a particularly large weighting of Naspers in their portfolios, this transaction presents an opportunity to consider whether now might be a good time to restructure one's portfolio:

Is this a good time from a valuation point of view to restructure? Investors may well have avoided this over the last year due to the belief that Naspers' valuation was at particularly depressed levels. In Figure 3 below, we show the share price as a multiple of expected earnings for Tencent, which accounts for >90% of Naspers's net asset value today. In 2018, Tencent's share price declined 47% from its January high, initially as part of a broad-based China Inc. selloff in response to the US-initiated trade war with China, and subsequently due to a freeze on new online game approvals by Chinese regulators. This price decline resulted in Tencent's valuation falling from what was admittedly a lofty 50x projected earnings to 25x projected earnings. The latter appears cheap when considered against Tencent's historic valuation range. Subsequently, as mobile gaming approvals have resumed and there has been growing optimism regarding a US/China trade deal, Tencent has recovered strongly and with it, Tencent's valuation. Now valued at 36x expected earnings, this is around the average based on the last 5 years.

Figure 3: Naspers share price as multiple for expected Tencent earnings



Source: Bloomberg, Anchor

Why would you not want a large concentration of exposure in Naspers in your portfolio?

Within the South African market, Naspers has been almost the only listed investment via which investors could play the technology growth theme, as well as having been a solid rand hedge. Its superior past investment performance notwithstanding, a nagging concern to consider – Naspers' overexposure to a single stock in a single market (Tencent in China), which accounts for >90% of Naspers' net asset value. As incredibly successful as Tencent has been, and still with compelling growth prospects ahead, the ban on new game approvals last year was a timely reminder of the risks posed by a heavy-handed regulatory environment in which Tencent operates. It suffices to say the first thought that runs through Chinese regulators' minds when they reach the office each day is not the interests of investors (particularly foreign ones). Such left-field risks can be mitigated by controlling the size of one's position in Naspers.

Are there viable alternatives?

A further concern that may have prevented investors from considering restructuring their Naspers investment into a fund has likely been that their exposure to the technology theme would be significantly diluted and thus risk underperforming Naspers going forward. Anchor has set up a dedicated global technology unit trust, which is expected to launch in June this year. This may be a worthwhile alternative to consider. This should be better balanced across more companies and countries.

When done for portfolio restructuring purposes, Section 42 of the Tax Act allows for rollover relief and no capital gains will be triggered because of the transfer of shares into a non-tax-sensitive fund. The current base cost will be rolled over and capital gains will only be realised on selling units in the fund.

In summary

Naspers's decision to list on Euronext may inadvertently have placed tax-sensitive retail investors with a set of rather unappealing choices. With Naspers' valuation no longer so cheap thanks to the strong recovery in Tencent, for those that might have been considering restructuring their portfolios anyway, it may be a worthwhile time to consider a Section-42 transfer to avoid being placed in this position, as well as to address single-stock/country exposure that one has through Naspers.

Wills, deceased estates and the process that follows ...

Di Haiden

As the saying goes, there are only two certainties in life: death and taxes! Unfortunately, often these two go hand in hand and most people have no idea as to what to do or what is expected when a death occurs. At RCI, with 37 years of looking after families and their wealth, we have built up a fount of knowledge as to what happens when someone passes away and the process that unfolds thereafter. Below, we highlight the main points of the process, which is usually complicated and lengthy, to give the reader an idea of what is involved.

Wills

The process starts (hopefully) with the drawing up of a will. If someone dies without a will, he/ she dies *intestate* and this makes the process even more complicated!

So, when do you need a will? When you have **assets** and **important people** in your life.

Why do you need a will? To leave your **assets** as you see fit to the chosen **important people** in your life.

When writing a will you need to consider the following: Who will inherit your estate, who will be the executor/s, will you establish a trust in your will and, if so, who are the trustees, what are your assets and do you want to leave anything in particular to one heir or a number of heirs? An individual must remember that a will can be changed at any time as you go through different circumstances and phases in your life so your first will is not necessarily set in stone.

Estates

An estate is the total of all your assets less your liabilities i.e. anything you possess in your own name less your debt or borrowings. What is not your estate? Very simply put, whatever is in a trust or a company that you have established.

Someone dies, what happens next?

The process starts as soon as there is a death. A funeral home is called in to prepare the deceased's body for burial or cremation and, most importantly, to obtain a death certificate from Home Affairs. The process of winding up an estate, can only start once a death certificate has been issued. In Figure 1, we show the important people involved in winding up an estate and below we highlight each person's role in the process.

Figure1: The people involved in winding up an estate

Source: RCI

You – This is the person responsible for making sure an estate is wound up. It is often a close family member or friend of the deceased.

The Executor is the person named in the will as being responsible for winding up the estate. An Executor has to be above 18 years of age, and You and the Executor may or may not be the same person. A professional institution such as a bank, financial advisor etc. can also be the Executor. If the deceased has nominated an individual then, upon date of death, that person may make use of a third-party to assist with the duties of an Executor of the estate.

Often the Executor appoints an **Administrator**, who is a professional at winding up estates. Since the process is specific and complicated it is preferable *not* to do it yourself.

The Administrator deals with the **Master of the High Court (Master)**, who is pivotal in approving the winding up of the estate. An estate cannot be wound up (except for very small estates), without the Master's consent.

As indicated by the flow of the circle in Figure 1 – **You** deal with the Executor, the **Executor** outsources the administration of winding up the estate to the **Administrator**, the Administrator deals with the Master, the **Master** reverts back to the Administrator who reports back to the **Executor**, who then comes back to **You** unless you are the Executor.

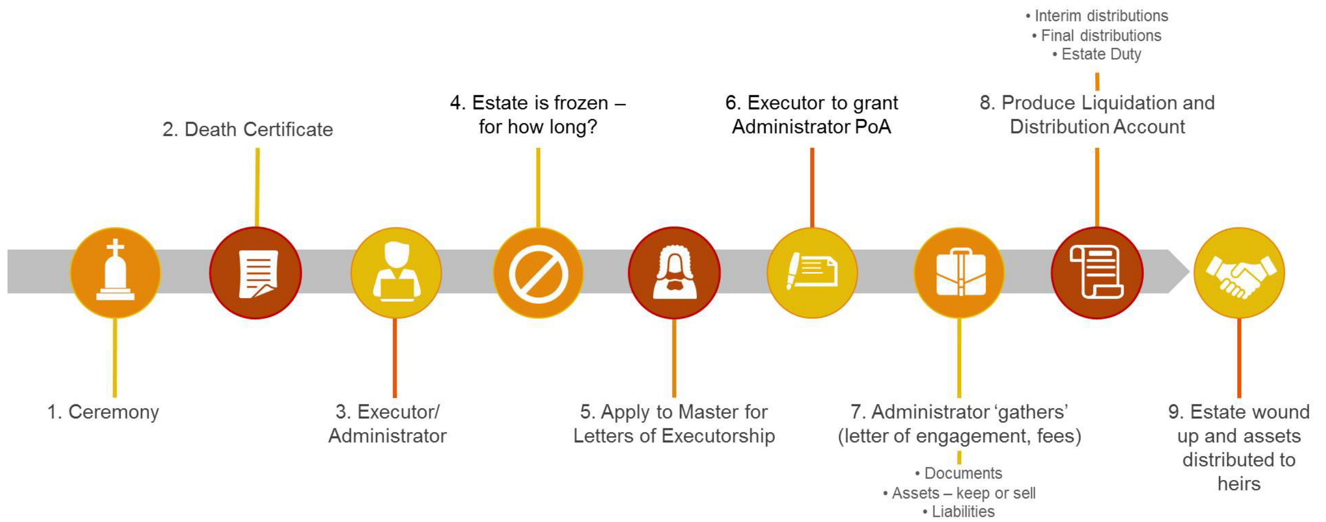
Essential documents in an estate

There are several documents required to start the process of winding up an estate as well as documents produced to finalise said estate. These documents include: A valid and original will, the death certificate and deceased's records are supplied by You, a letter of executorship from the Master, The SA Revenue Service (SARS) provides a tax-clearance certificate after tax returns have been submitted and the Executor lodges a Liquidation and Distribution (L&D) account, drawn up by the Administrator, with the Master.

Timeline

Currently, the time taken to wind up an estate in Gauteng is c. two years. In Figure 2 and below, we summarise the sequence of important events:

Figure 2: Sequence of important events



Source: RCI

1. The burial ceremony of the deceased takes place.
2. A death certificate is issued by Home Affairs.
3. The Executor/ Administrator starts winding up the deceased's estate.
4. The estate's assets are frozen from the time of death until the Master issues a Letter of Executorship. Once issued, interim distributions may be permitted by the Executor.
5. The Administrator applies to the Master for the Letters of Executorship to be issued (currently it takes 4 months).
6. The Executor gives the Administrator a power of attorney (POA) to wind up the estate.
7. Once letters are issued the Administrator 'gathers' all assets, liabilities etc.
8. The Administrator then draws up the L&D Account, which is submitted to the Master.
9. Once there are no objections, and the Master approves the L&D account, the estate is wound up and assets are distributed to the deceased's heirs.

Costs

There are several fees/costs to be paid by an estate:

1. Executors' fees: There is a statutory fee of 3.5% of the estate's value charged by the Administrator.
2. A final tax amount (of the deceased) has to be paid to SARS.
3. Estate duty: The first R3.5mn of an estate is exempt from estate duty, however, from R3.5mn to R30mn is taxed at a rate of 20%, while R30mn-plus is taxed at 25%. If a spouse inherits, no estate duty is payable until that person's death and the R3.5mn rolls over to the surviving spouse.

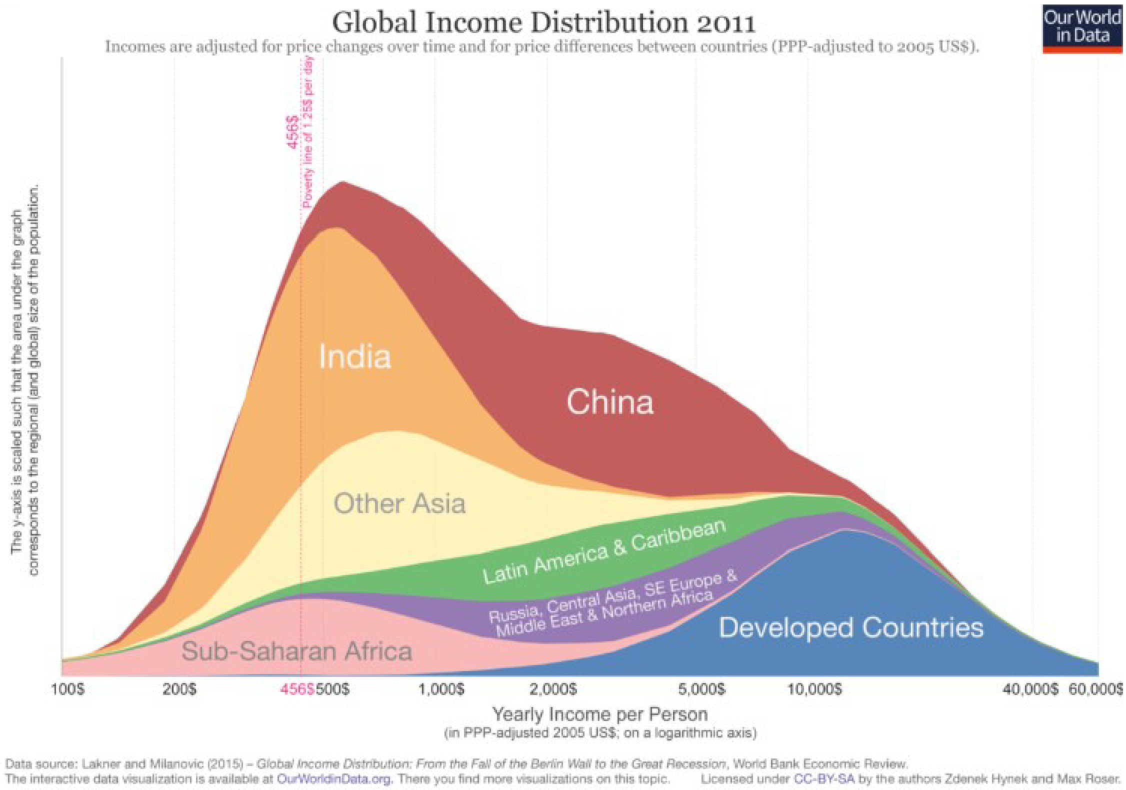
What can RCI do?

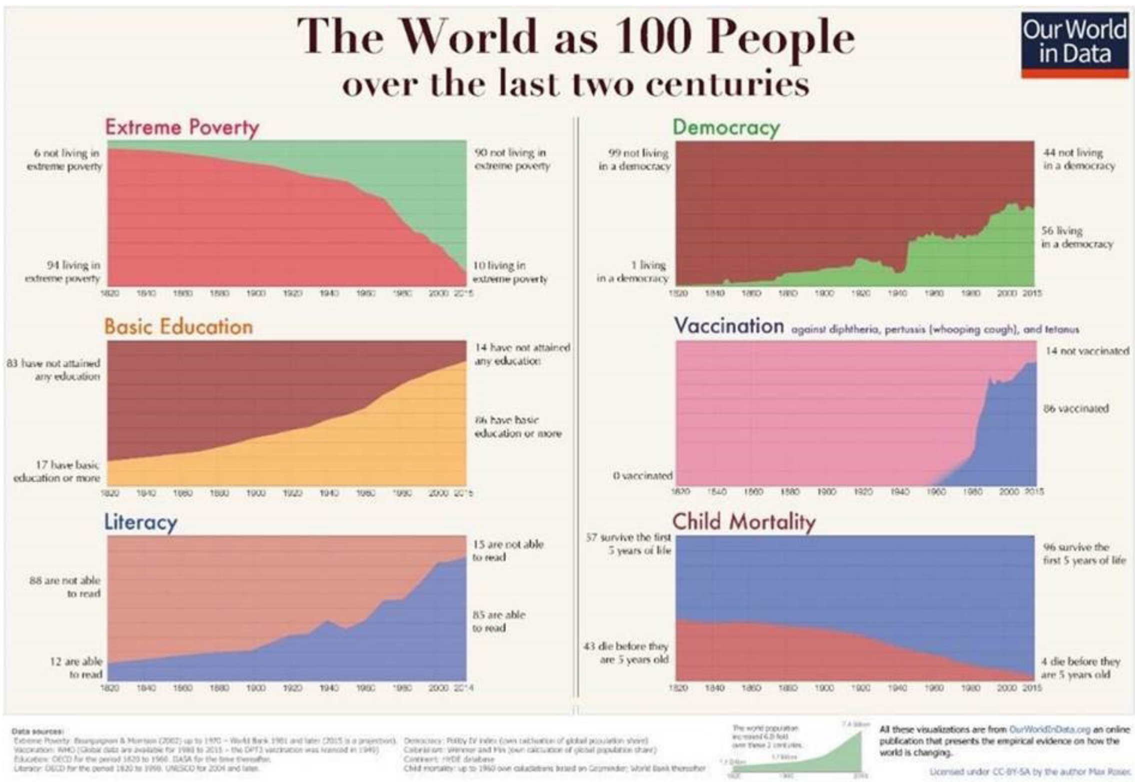
1. We run the process for you – this entails dealing with **you**, being the Executor and/ or dealing with the Executor/ Administrator and ensuring that progress is made in winding up the estate as timeously as possible.
2. We also negotiate the Administrator's fees and we try to reduce this cost.
3. We create a legacy file to hold all relevant information related to the deceased's estate.

We understand the people involved in a deceased estate and the process but, most importantly, we know how money works in winding up an estate. We have found that each person's situation is unique, and one needs to understand how all the above applies to your individual circumstances.

In this note we have only scratched the surface of a very complex subject so we would suggest contacting RCI directly if you would like to have a conversation about any of the above-mentioned processes.

Don't get depressed, the world improved hugely over the past century





Ignore the Brexit scare stories - they have no basis in sound economics

From Fuller Treacy Money, 2nd April

https://www.independent.co.uk/news/business/comment/brexit-scare-stories-ashoka-mody-imf-bank-of-england-mervyn-king-economics-trade-a8670416.html

Thanks to a subscriber for this article by Ashoka Mody for The Independent. Here is a section:

As Krugman wrote in a brilliant 1995 essay, "People believe certain stories because everyone important tells them, and people tell those stories because everyone important believes them. Indeed, when a conventional wisdom is at its fullest strength, one's agreement with that conventional wisdom becomes almost a litmus test of one's suitability to be taken seriously."

British leaders must pull themselves out from the spell of storytelling and focus on their urgent responsibilities. At home, they must heed the real message of the Brexit vote: citizens being left behind by globalisation are clamouring for more protection. Prime minister Theresa May seemed briefly to recognise the primacy of that task. But she was sucked quickly into the Brexit negotiations vortex.

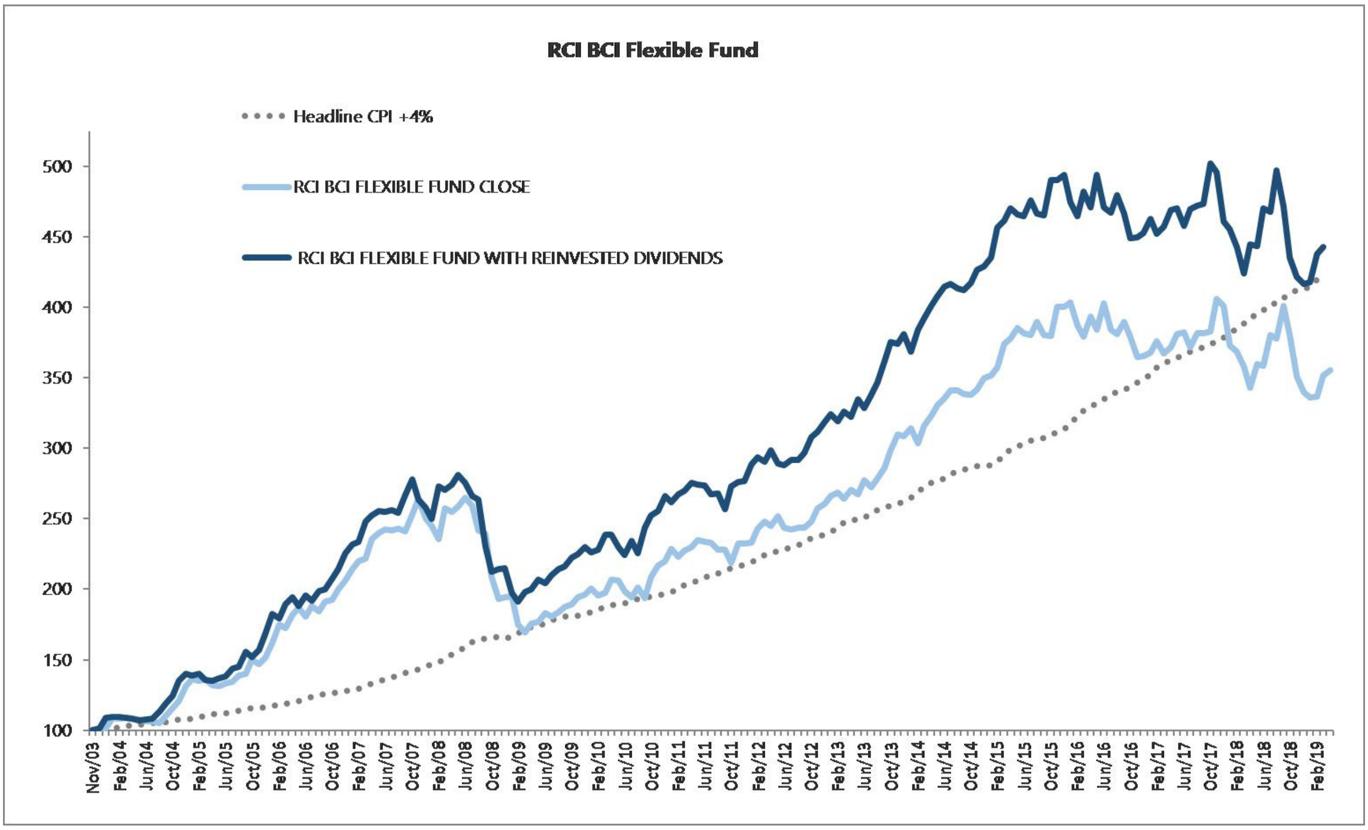
On Brexit, British citizens and their leaders must decide what kind of nation they want to live in. The debate must pit the value of sovereignty against the risks to global peace. Such a debate is of the utmost importance for Europe, with its history of horrific wars, especially now when ugly forms of nationalism are gaining alarming numbers of adherents. Unfortunately, instead of dealing head-on with this monumentally important challenge, which must guide the Brexit decision, global leaders are peddling frightening economic scenarios.

The Remain or Leave decision is an opportunity for Britain's citizens to express and reaffirm their true values. Failure to protect the most vulnerable at home and redirect the Brexit debate to a higher purpose will leave underlying tensions simmering.

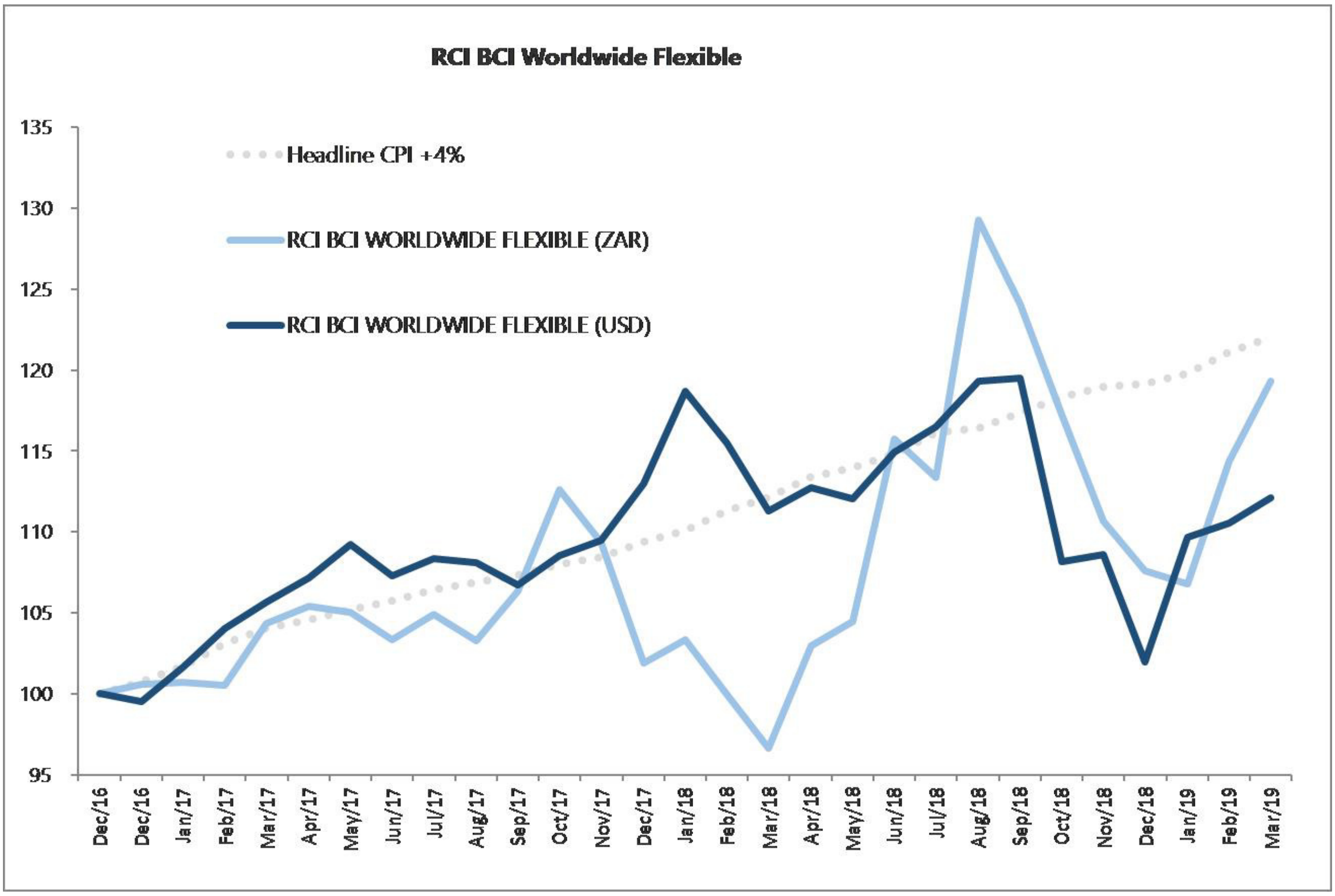
RCI Unit Trusts

Please contact Maggie on 011 591 0578 for any help on your unit trusts.

RCI BCI Flexible Fund closed March at 355.18c, up 1.7% for the month and 6.39% for the year to date. For South Africans, March will probably be remembered for the 10 consecutive days of power cuts. As anxiety grew about the economic impact of these outages and risks of further disruptions as SA heads into the seasonally high power demand winter months, the possibility that this may tip Moody's into downgrading SA's credit rating to junk in its review due at the end of March loomed. Against this backdrop, domestic consumer stocks and interest rate sensitive financials bore the brunt of the negativity. The rand weakened 2.9% vs. the US dollar in March, supporting resources and industrial shares that have a large component of offshore earnings. This rand hedge support mitigated much of the damage felt by domestically focused shares, with the FTSE/JSE Capped SWIX Index down 0.2% on a total return basis for the month. This lagged global markets, however, with Developed Markets and Emerging Markets delivering a positive total return in US dollars of 1.4% and 0.9% respectively in March.



RCI BCI Worldwide Flex closed March at 119.33c, up 4.3% for the month and 10.92% for the year to date. It is up 23.8% for the past 12 months! You can see why we have kept saying 'live local but invest global'!



Unit trust has flexibility – happy to take small amounts

The unit trust has the flexibility to buy and sell shares and to change weightings more frequently than in an individual portfolio. We are happy to take small amounts into the unit trust (from R1 000 per month or lump sums of R25 000). As you will not pay commission to any agents there is no cost to get in and out of our fund. On selling, the amount you receive back will depend on our performance.

To conclude

The practise of investment is boring to some clients. It is about doing the 'right thing', day in and day out for many years. Sometimes, it takes ages for a plan to come together. For many years, we have warned that South Africa is likely to be downgraded to junk status at some point in the future. At that point, all the rating agencies considered South Africa to be of investment grade but to us the stars were beginning to misalign. We warned that it was fairly easy to take the correct steps to maintain our investment rating but, as a country, we were unlikely to take the unpopular actions required to stave off the problem.

Two of the three rating agencies already consider us junk but the third has again given us a stay of execution. Viva! The risk of turning to junk over the next two years is now very high. We do not derive joy from our country slipping down the slippery slope, but we consider it almost inevitable – and invest accordingly.

Thus, we have stuck to this boring, depressing theme because the risks continue to manifest. It is not nice to have to ring the alarm bell, but someone has to do it. In the short-term, we are only a month away from the election. Thereafter, South Africa can get back to work, so we are hopeful that we have seen the bottom in the economy and local share prices for the next while.

We hope to be the best family office in the country!

Best regards

Di, Alan and Mike