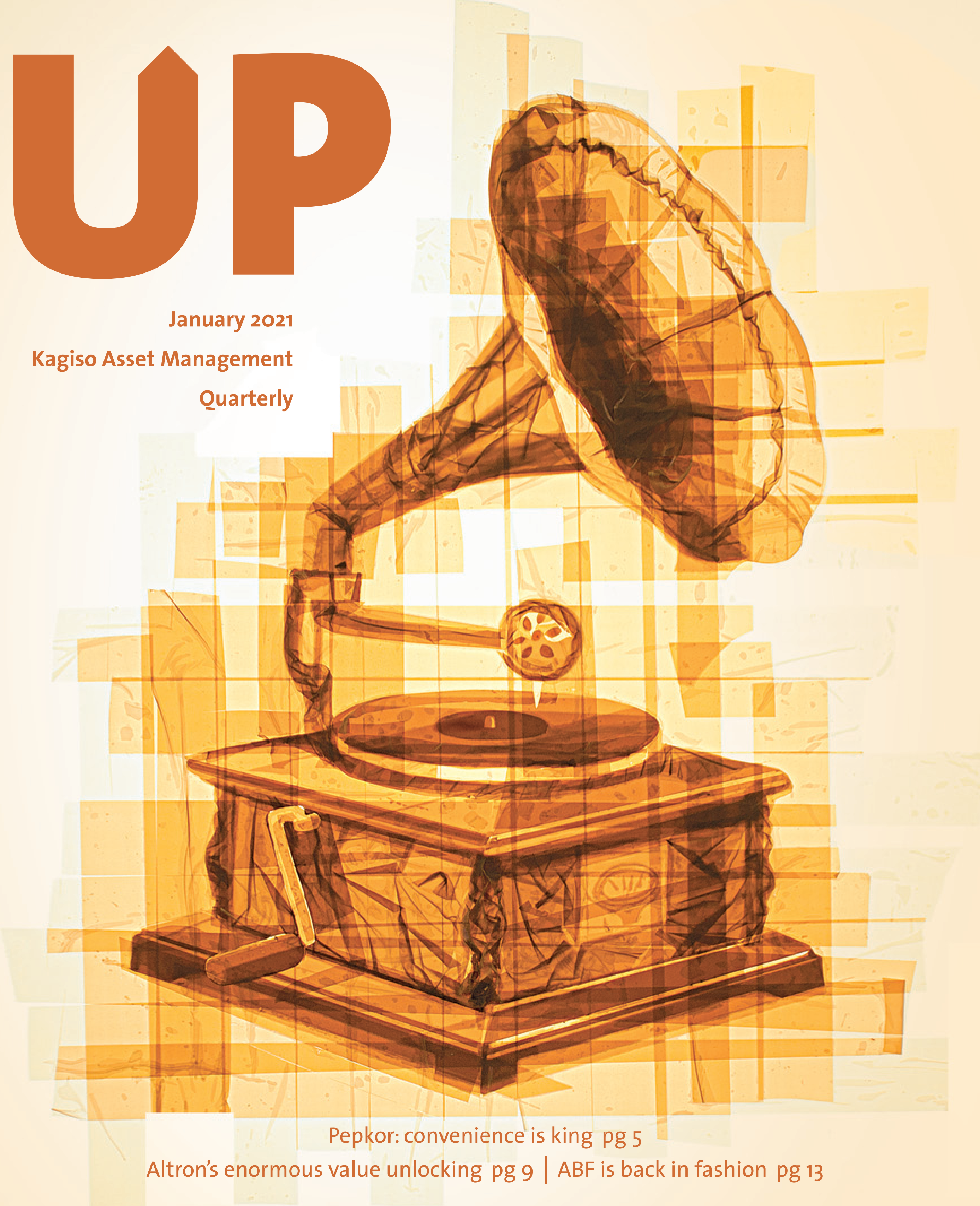
UP

January 2021

Kagiso Asset Management

Quarterly



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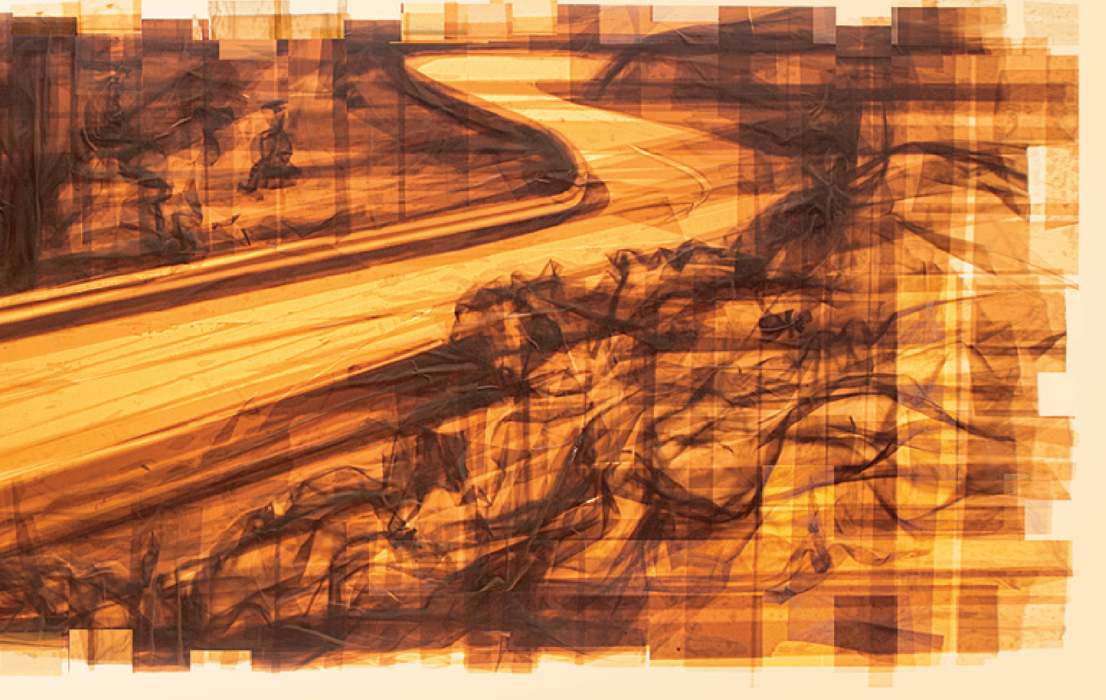


Equites: enabling modern logistics

Sheldon Kisten - Investment Analyst

"Equites Property Fund is the only specialist logistics Real Estate Investment Trust (REIT) listed on the JSE Securities Exchange, with a healthy track record of owning, developing and operating world-class properties in South Africa and the UK.

We unpack Equites' promising prospects, focusing on evolving supply chains and the impact of global e-commerce developments."

Equites: enabling modern logistics

Superior asset base attracts quality tenants

Equites develops property assets according to client specifications, with a view to either rent the property to the client on a long-term basis or, in some cases, develop it for the client - profiting from the difference between the actual cost of the development and the agreed price.

Since listing in 2014, the company has grown its portfolio value from R1 billion to over R16 billion - R10 billion of which is based in South Africa. The remaining value is in the UK portfolio, which is currently growing faster than South Africa's.

Equites' well located, modern and recently built warehouses have attracted top-quality tenants including large retailers, consumer and industrial goods companies, and logistics service providers. Their tenants include: Amazon, DSV, DHL, Pick n Pay, Tesco, Foschini, Medtronic, Cummins, Imperial and Puma.

Longest leases in town

Equites currently boasts the longest weighted average lease expiry (WALE) profile among South African-listed property companies. This provides an indication of the future security of income streams to investors by measuring the average time period over which leases in a property portfolio will expire. A longer WALE indicates lower risk and this results in lower cost of capital from banks and other funders. The WALE across Equites' entire portfolio is in excess of 10 years, biased towards longer dated lease expiries in the UK. This contrasts an average WALE of approximately four years for South African cohorts.

Equites' leasing strategy is a key component of the business. Tenants are signed on triple net leases, whereby the tenant pledges to pay for all property-related expenses (ie taxes, insurance and building maintenance costs) over and above the rental amount. By shifting the responsibility of property maintenance to the tenant, cash flow for this does not need to be factored in when determining annual distributions. This enhances Equites' ability to pay out distributable earnings to shareholders relative to other REITs and they are able to target close to a 100% payout ratio.

Key facility requirements of modern logistics

Traditionally, industrial properties were characterised by large, empty warehouse spaces used predominantly for storage. It is difficult and often impossible to convert traditional warehouses to the modern specifications required by tenants today. Equites is therefore able to attract tenants from old-style warehouses and accommodate new tenants who will only occupy a modern space. Being one of the few REITs who have in-house development capabilities, Equites can tailor warehouses according to the tenant's needs, resulting in them becoming a preferred developer and landlord.

Modern logistics warehouse specifications incorporate:

- **Automation** has become central to each build. The *left picture on the next page* illustrates a general build by Equites, where emphasis is placed on the height of the building (increased storage capacity), the yard space (more efficient entry/exit and parking of delivery vehicles) and automation systems such as those used for storage and retrieval. Typically, these systems comprise of automated forklifts, conveyors and pallets that work together with warehouse management software to store and retrieve goods as desired *(right picture on next page)*.

- **Environmental considerations** are very important to businesses today and the incorporation of solar roof panels, water storage tanks and electric vehicle (EV) charging stations in modern warehouses is increasingly commonplace. Equites recently signed a deal with Amazon to develop a 14 000 m² warehouse in the UK, which will include a multi-story parking facility comprising hundreds of EV charging stations, accommodating the UK's urgent move away from internal combustion driven transport.

- **Location** is an essential consideration in logistics planning to optimise supply chain efficiency. Equites' warehouses are typically surrounded by excellent transport infrastructure, predominantly located in areas that have easy access to highways and main roads. This allows for greater efficiency in transporting goods in and out of storage, and better working capital management.

Evolving supply chains for retailers

Supply chain management involves the movement, storage and end-to-end order fulfilment of raw materials, work-in-progress inventory and finished goods. Mastering this is an integral part of gaining a competitive edge and optimising returns on capital for all companies distributing products.

For retailers, stock would traditionally be stored at the back of a store, easily retrievable when needed. The shortcomings of this approach include having to carry considerably more stock as a whole to prevent outages, and the costly movement of stock from store to store. Consequently, retailers are progressively using a more centralised supply chain model, where less stock overall sits in a single warehouse and is distributed to various stores as demand dictates.

Era of e-commerce

'Last mile delivery' refers to the final journey that goods embark on to get to the end customer. As online retailing grows, retailers are increasingly offering the service of goods delivery directly to the customer, removing the need for in-store shopping or collection - another reason for retailers to move to a centralised supply chain management system. Landlords and operators of logistics assets in particular, benefit from this shift, in the UK and progressively in South Africa.

Consequently, the demand for logistics warehouses that was originally driven by logistics companies, is now also buoyed by traditional retailers offering online shopping, and pure online retailers.

Despite double-digit growth for many years, online sales in South Africa (as a percentage of total retail turnover) still lags many parts of the world at 2%, whereas the UK boasts the third highest levels of global e-commerce penetration at 18%. Recent experience during pandemic lockdowns has been materially higher too.

Established online retailers such as Amazon and Takealot are highly dependent on the logistics sector for the fulfilment of orders and the provision of warehouses as centralised storage and distribution centres. They are increasingly building their own distribution networks and renting their own modern logistics facilities.

Growth is best served organically

Equites have displayed a tendency to manage their balance sheet conservatively, often favouring equity capital funding over debt. This is evidenced in the *chart on the following page*, which shows that the company has the second lowest loan-to-value (LTV) ratio across the South African listed

General warehouse build by Equites

Source: Equites

Modern logistics automation systems

Source: Interlake Mecalux

Equites: enabling modern logistics

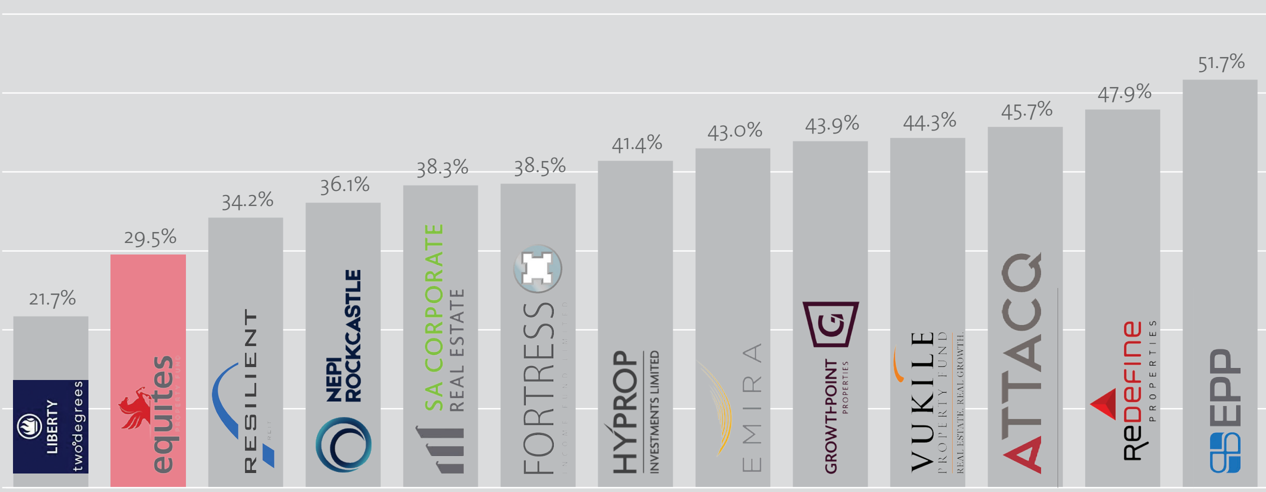
property sector. A lower LTV ratio is a key indicator of lower financial risk and greater financial flexibility. It is particularly important in tougher economic times when receipts from tenants may decline.

Equites recently teamed up with experienced UK logistics developers, Newlands Property Developers, to form the Equites Newlands Group. Equites are majority shareholders in this joint venture, allowing them to determine the end-use of the development (ie develop for a client at a profit or retain and let). Equites provides the capital, while Newlands sources the land and tenants. Profit is shared, with Newlands required to reinvest a portion of the profit back into the venture. Recent deals concluded with Amazon and Hermes are early evidence of a promising future for this joint venture.

Solid footing presents sound growth potential

Equites offers pure exposure to a high potential, niche property sector in logistics, in an environment where many of the listed South African REITs are struggling with excess inventory and reduced demand for space. They have a robust portfolio with a long WALE and low LTV. The portfolio is expanding apace through the addition of well-positioned, high-quality property assets that include excellent lease agreements with established, big-brand tenants. Equites' assets offer geographical diversification and exposure to the logistics property market that is set to thrive in the medium to long term, locally and in the UK. UP

Reported loan-to-value



Source: company reports, Investec Securities estimates

Pepkor: convenience is king

Sarah le Roux - Investment Analyst

"Pepkor is a South African retail investment holding company whose most valuable assets are PEP and Ackermans, two of the country's most successful clothing retailers. We take a deep dive into the operations of these retailers, unpacking the techniques employed to steadily expand their businesses and deliver value to customers."

Pepkor: convenience is king

Pepkor at a glance

Pepkor is structured into four operating segments: clothing and general merchandise (CGM); furniture, appliances and electronics (JD Group); FinTech; and The Building Company (TBC).

TBC is in the process of being sold to Cashbuild, a competitor within the building supplies sector, with final Competition Commission approval expected in March 2021. The charts that follow therefore exclude this segment.

The organisational *chart below* illustrates the brands that lie within each of the remaining three segments. The CGM segment is further divided into PEP and Ackermans (South African stores only), Speciality and PEP Africa (PEP stores outside of South Africa), with the Speciality division housing smaller clothing and footwear retail brands. Within FinTech, Flash provides point of sale (POS) technology enabling virtual products such as airtime and electricity to be sold in the informal market, and Capfin is a short-term unsecured credit provider.

The contribution *charts on the following page* demonstrate that the CGM segment and, within that, Pep and Ackermans, is responsible for the bulk of Pepkor's revenue and profits. Although the JD Group has been loss-making for several years, performance has been steadily improving as the store base has been reduced. This segment is expected to break even from the 2021 financial year and to have a marginally positive contribution thereafter.

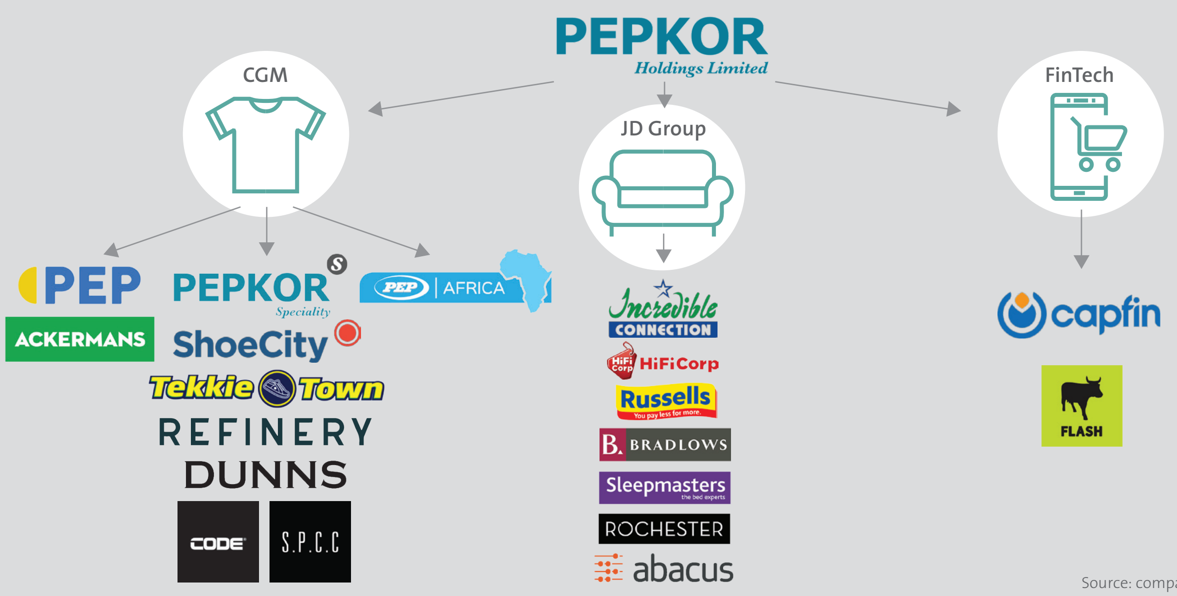
Enduring brands

Ackermans opened its first store in 1916. Over a century later, there are 861 stores countrywide that primarily target women with children in their lives. Kids and baby clothing accounts for over 60% of sales, with roughly a 20% contribution from womenswear and the remainder from cellular devices, airtime and fast-moving consumer goods (FMCG) including essentials like basic toiletries and nappies.

PEP has been operating for 55 years and has expanded from clothing into homeware, cellular devices and airtime, FMCG, financial services and parcel delivery. The 2 384 stores countrywide include more than 250 PEPhome stores that offer a range of homeware items and over 500 PEPcell stores that sell airtime and cellular products (including PEP's own exclusive brand of cellular handsets and accessories - Stylo). A new discount variety store format known as Dealz is also being trialled, with 15 stores at present. PEP clothing stores comprise the remaining outlets, selling a quarter of all kids clothing and almost a third of all baby clothing in South Africa[1].

[1] According to June 2020 data from the Retail Liaison Committee (RLC).

Pepkor organogram



Source: company presentations

Strategic positioning

PEP primarily targets lower LSM[2] customers with very little disposable income. The store network has been designed around customer convenience, with the aim of lowering transport costs to reach stores, thus maximising potential spend. PEP prides itself on price leadership, with 97% of all products priced either the same or cheaper than at any other retailer. Ackermans' price points are generally higher than those of PEP, however they are also classified as discount retailers. Store sizes range from 200 to 2 000 m² across both brands. The ability to profitably operate a wide range of store formats has led to a significantly larger network of stores than competitors, with room for further growth.

The clothing offering of PEP and Ackermans is centred on basics - items that can be worn from one season to the next, independent of current fashion trends. As the product has minimal risk of losing relevance, it is possible to buy in bulk with long lead times of up to nine months, thereby bringing down the unit cost of each item purchased. The longer shelf life of basics relative to fashionable clothing also reduces the need to rely on markdowns to clear stock, aiding ultimate profitability. Margins have remained relatively constant in this division, with efficiency gains in the supply chain invested back into price or improving quality to increase the attractiveness of the offering over time.

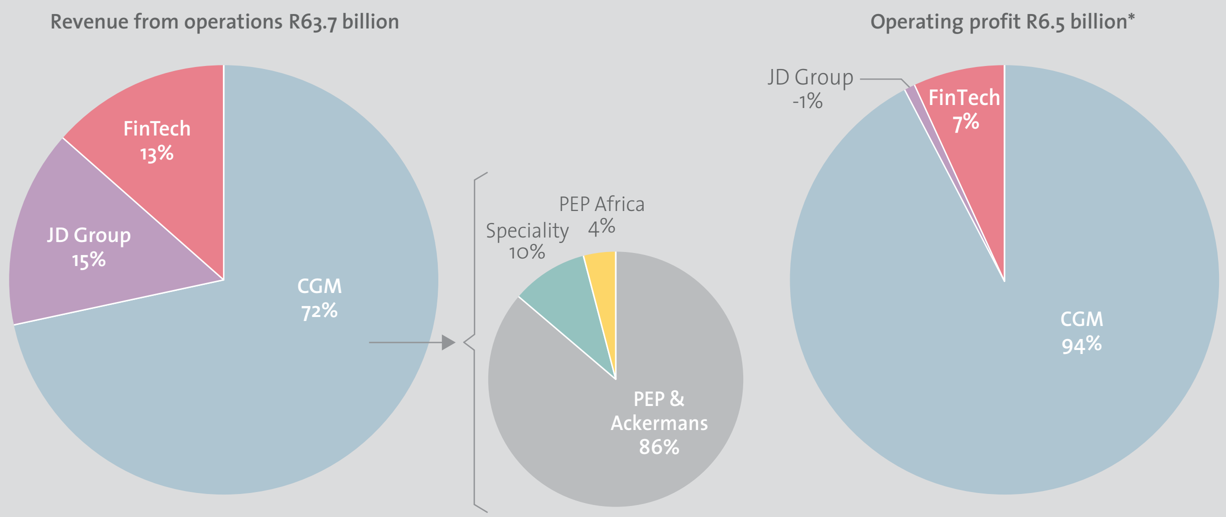
Leaders in schoolwear

PEP sells more than half of all school clothing sold in South Africa[3]. These garments are predominantly locally manufactured by Pepclo, a clothing manufacturer owned by the Pepkor group. Employing more than 2 000 people, it is the largest South African clothing manufacturing facility operating under one roof. Pepclo currently manufactures around 15 million units per year, including basic schoolwear (excluding school shoes), flip-flops, basic underwear and, more recently, masks and disposable isolation gowns.

Between 20% and 30% of school clothing sales occur in the "back-to-school" period, from just after Christmas until schools open. To capture the maximum amount of spend, store inventory is rapidly shifted from Christmas to back-to-school within a three-day period directly after Christmas. During this time, up to 30% of store space is allocated to schoolwear, compared to 3% to 4% over the remainder of the year.

[2] Living Standards Measure (LSM) has become the most widely used market segmentation tool that cuts across race, gender, age or any other variable used to categorise people.
[3] According to March 2020 data from the RLC.

Pepkor segmental contributions to revenue and operating profit (2020)



*Calculated before impairments
Source: company reports, Kagiso Asset Management estimates

The bulk of the schoolwear inventory required over this period is built up in distribution centres in the months leading up to Christmas, with a smaller proportion manufactured during the back-to-school period. Local production mitigates risks around lost sales due to inventory delays, reducing both the length of time and the amount of space needed to store this inventory. Again, the focus on basics proves to be an advantage as there is limited risk of inventory write-downs on the stock that is temporarily removed from stores to make room for a greater proportion of schoolwear.

Leveraging an extensive geographic footprint

Stores are generally replenished at least twice a week and, in some cases, more frequently depending on the size and popularity of the store. Regular store replenishment allows for smaller store formats as less inventory is required to be kept on hand. Moreover, it has enabled the group to leverage the store footprint and supply chain to create new business lines. In 2018, PEP launched a parcel delivery service called PAXI, whereby customers can send parcels from one PEP store to another. Competitive pricing and a store network that significantly outstrips the number of South African Post Office outlets has led to PAXI already delivering around 10 000 parcels daily.

The FinTech division of Pepkor has also benefitted from this extensive footprint. Customers can apply for Capfin loans in PEP and Ackermans stores. In addition, vendors in the informal market can buy Flash POS devices along with the tokens required to top up these devices. Other financial services offered in store, falling outside of the FinTech division, include account payments (eg DStv), funeral cover and money transfers. The select range of essential FMCG products on offer across both retailers encourages impulse buying that assists in increasing the average customer basket size. The net impact of all these offerings is a more profitable use of space and added incentives for customers to visit stores more frequently.

Resilient business model

Despite the impact of COVID-19, Pepkor was able to grow sales across all divisions apart from TBC in the financial year ended September 2020. Strong free cash flow generation and good working capital management assisted in paying down a substantial portion of their debt, reducing potential liquidity concerns. With the sale of TBC on the horizon and the rightsizing of the furniture and electronics store base essentially complete, the business is in a strong position to meaningfully grow earnings in 2021 and the years to follow.

Looking ahead, South Africa has weak economic fundamentals, with unemployment expected to remain high and consumer incomes under pressure. Most lockdown-related job losses occurred in the lower income segment, leading to reduced disposable income and consumer downtrading. Consumer spend has also shifted towards convenience, with customers choosing to shop closer to home. Though risks remain in this environment, Pepkor's positioning as a discount retailer with stores located close to their customers appears well placed relative to competitors. As such, we view Pepkor as best positioned of the local clothing retailers to weather the current tough operating environment.

Altron's enormous value unlocking

By Meyrick Barker - Investment Analyst

"The Allied Electronics Corporation (Altron) has been significantly reconfigured over the past five years, initially focussing on a reset of cost structures and the disposal of manufacturing-intensive businesses. The strategic focus was then shifted to information and communication technology (ICT) related businesses."

Altron's enormous value unlocking

The recent unbundling of their UK ICT-services company, Bytes Technology Group (Bytes UK), highlighted that the inherent value of this asset was underappreciated by the market, given the low Altron share price. Substantial value has been created for Altron shareholders by this turnaround, and the separation and unbundling of Bytes UK.

Corporate history

Bytes UK was founded in Epsom, south of London, in 1982. It made its way into the Altron stable via USKO, a business listed on the JSE in the late 1990s. Altron acquired a 20% stake in USKO in 1999 before buying out and delisting the company a few years later.

USKO and Altron had similar journeys: poor capital allocation, unsustainable debt levels and underperforming businesses that resulted in stressed operations. The injection of new management teams enabled the businesses to refocus and extract the value inherent within.

Acquired for R145 million in 1998, Bytes UK was notably one of USKO's more successful acquisitions. Having subsequently bolstered the original Bytes UK business with a relatively small acquisition in 2011 (Security Partnerships), followed by a larger transaction of around R650 million in 2017 (Phoenix Software), Bytes UK was unbundled from Altron and listed separately on the London and Johannesburg Stock Exchanges in December 2020. It now has a market capitalisation in excess of R17 billion.

Unlocking value

The unbundling of Bytes UK was structured so that Altron shareholders directly retained approximately 60% of the original stake, with roughly 20% thereof sold for cash in the listing and distributed to Altron shareholders. The balance was sold down by Altron to pay for taxes that arose from the transaction and to reduce debt. In addition, a portion was allocated to Bytes UK management to replace a pre-existing incentive scheme. Altron shareholders were given the option to sell their entire stake on listing.

The intention of the unbundling was to unlock value for shareholders by improving the visibility of the earnings and cash generating ability of Bytes UK, and gain exposure to a broader potential shareholder base. As a separately listed entity, the company has renewed focus and energy along with greater flexibility to use Bytes UK's scrip for talent retention and corporate actions. The share price of Bytes UK has substantially rerated as a separate entity, massively benefitting Altron shareholders.

Implementing workplace IT solutions

The workplace is rapidly evolving, with distributed teams, new business models and complex security issues resulting in evolving software requirements. Bytes UK is a value-added reseller (VAR) working with corporate customers to identify and attend to their developing software needs. Through a deep understanding of the technologies available to aid businesses transition accordingly and improve productivity, Bytes UK sells the appropriate software licenses to clients. Its primary focus is on cloud[1] and security products, including providing advice regarding updates or optimisations to existing software and helping to manage licence compliance and renewals.

In addition, managed service offerings are provided, such as the scalable extension of an in-house IT team to augment internal expertise and offer support to staff. This can also include assistance with technical projects (for example designing, implementing, supporting and managing a data centre solution) and the procuring of necessary software and hardware. Some of this work is outsourced to preferred service partners under Bytes' brands.

Bytes UK's client base is evenly split between the private and public sector (including municipalities, charities, healthcare and law enforcement), with public sector work typically being lower margin but longer term in nature and less impacted by economic contractions.

The UK IT market is highly price competitive and fragmented, with no single UK VAR having greater than a 7% market share. Bytes UK is the 10th largest UK VAR and managed service provider. Although it has a broad geographical presence in the UK, public sector exposure is largely concentrated in the North, while private sector business is conducted mainly in the South. Generating revenues in the region of £400 million per annum, the company enjoys a reasonable market share, with room for growth.

[1] The practise of using external processing, software and data storage resources.

VARs earn rebates from vendors based on numerous factors including the volume and growth rates of sales and their technical prowess and service levels (accreditations and certifications held). Generally, a VAR receives better commercial terms from a vendor through the attainment of higher levels of accreditation. Bytes UK has received numerous awards from vendor partners.

While best known for their expertise in Microsoft solutions, the company's offerings extend well beyond this, as can be seen by their partnerships with over 100 global vendors including Adobe, Amazon Web Services, Dell and HP. Microsoft is, however, their largest vendor, accounting for 52% of sales - generating more than $1 billion of revenue for Microsoft annually.

Why would IT users and vendors use VARs?

Approximately two thirds of IT spend in the UK is directed through distributors or resellers. Bytes UK is vendor neutral and therefore able to recommend the most appropriate IT offering from multiple providers based on a customer's specific needs - acting as a single touchpoint for multiple IT solutions. Typically, customers do not have the in-house capabilities to source and manage all their IT requirements. VARs are frequently able to offer more competitive pricing than a customer can attain directly from a vendor, given the preferential commercial terms VARs receive. The quality of technical expertise and guidance that Bytes UK can offer, coupled with the calibre of their personnel, is critical to the success of the business. To date, the company has successfully maintained a stable workforce, retaining and growing skills from within. The *chart below* highlights the strong correlation between staff tenure and profit generation.

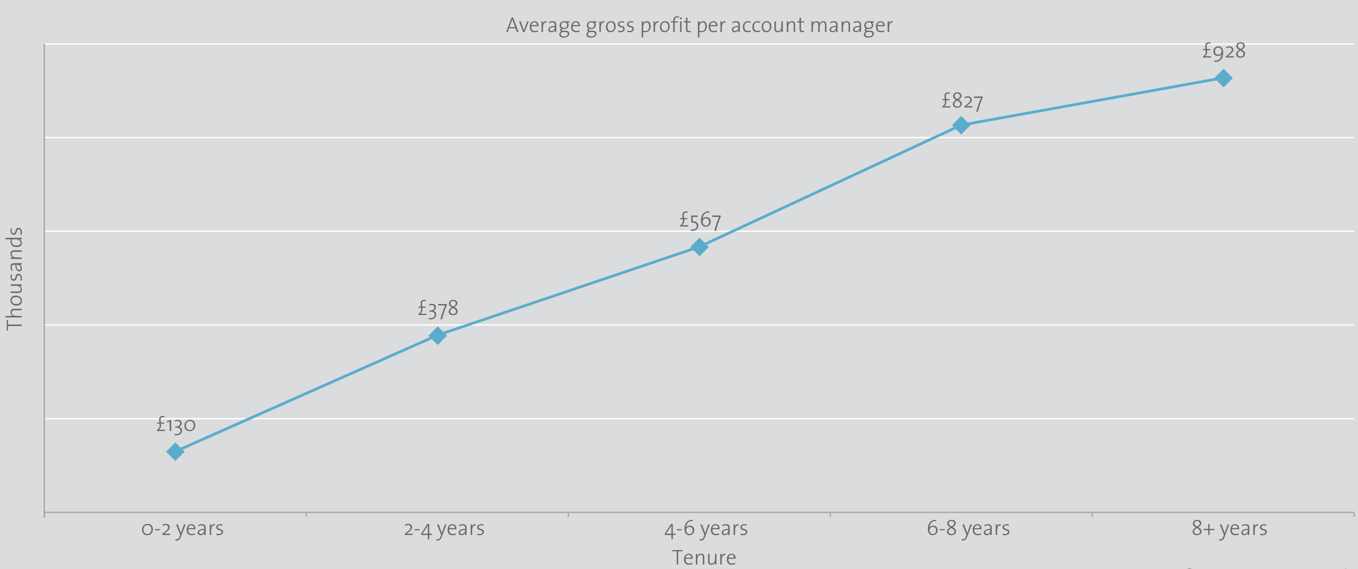
From a vendor's perspective, Bytes UK can:

- provide access to a broad customer base;
- offer a large sales contingent to promote products;
- mitigate the credit risk of dealing with many smaller customers;
- provide ongoing training and advice on new products to customers; and
- source valuable customer feedback for future vendor product development.

Forging a strong growth path

Bytes UK has a long track record of delivering robust financial performance (*charted on the next page*). As sales staff improve their understanding of the customer and progressively gain their trust, they are better able to identify additional, higher value solutions well suited to the customer's needs, resulting in increased IT spend.

Retaining sales staff proves highly profitable



Source: company reports

Altron's enormous value unlocking

The growing digitisation of operations is a structural driver that underpins Bytes UK's continued growth. As companies seek to communicate more effectively (internally and with customers), streamline business processes and grow operations, increased IT spend on software solutions is invariably a consequence.

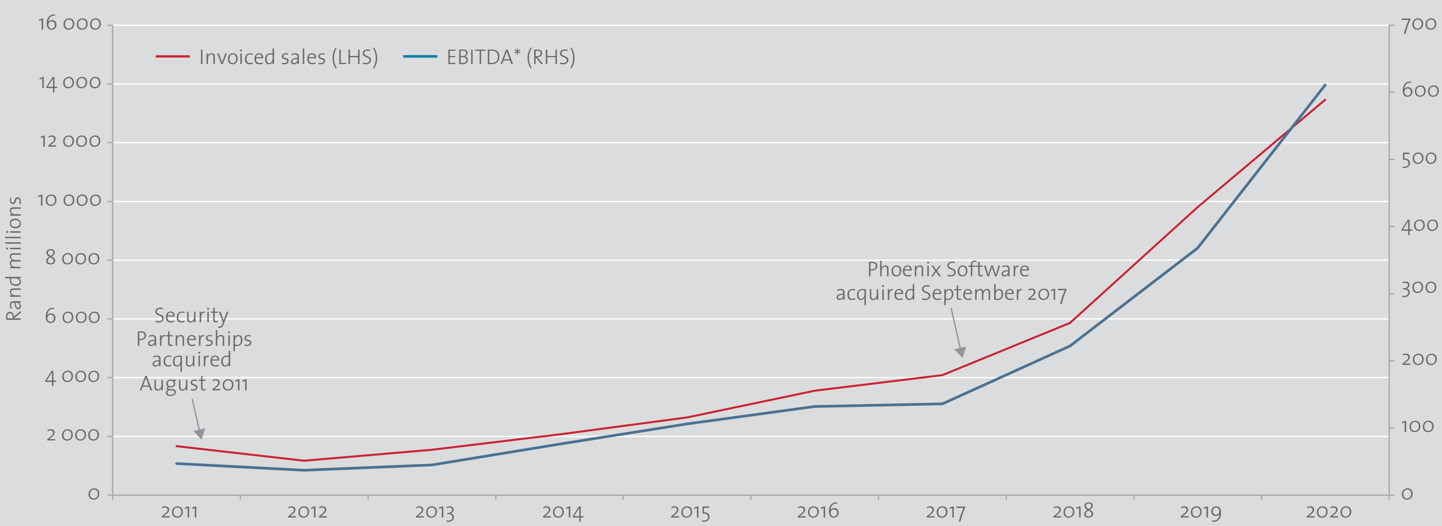
Bytes UK is well positioned to capitalise on the shift of workloads and services to the cloud, and the increasing threat of cyber security breaches. The need to support mass home working resulting from the COVID-19 pandemic, has accelerated the demand for cloud services. The shift to cloud is particularly beneficial for Bytes UK as it increases the proportion of profits generated from annuity-type revenue streams. Although sales teams are actively incentivised to boost the proportion of cloud sales, they also focus on cutting through the hype, helping customers identify which aspects of their business should be migrated to the cloud (and in what order) and practical uses of the available applications.

Cloud vendors have complicated usage-based pricing models, which can result in customers unknowingly breaching the terms of their licences or receiving an unexpectedly high bill at month-end due to usage exceeding expectations. As such, Bytes UK has developed an innovative system to easily monitor live consumption, helping customers minimise costs. Prominent customers include IKEA and Diageo.

Currently, the business has minimal presence in the IT hardware sales market. To mitigate the risk of competitors supplying hardware to customers and then cross-selling other products once becoming the hardware supplier of choice, Bytes UK are gradually expanding their hardware offering.

As outlined above, it is clear that Bytes UK is well positioned to capitalise on a number of opportunities that will deliver solid earnings growth. Our clients have substantially benefited from our holding in Altron over the past five years and we were supportive of the recent unbundling. UP

Cloud adoption delivering strong sales growth



*Earnings before interest, tax, depreciation and amortisation
Source: company reports

ABF is back in fashion

Dirk van Vlaanderen - Portfolio Manager

"In 1935, Garfield Weston sought to expand his family's already successful Canadian baking business by acquiring seven bakeries in the UK. This proved to be just the beginning of a bigger journey, culminating in the global food processing and retailing group known today as Associated British Foods (ABF), operating in 53 countries."

ABF is back in fashion

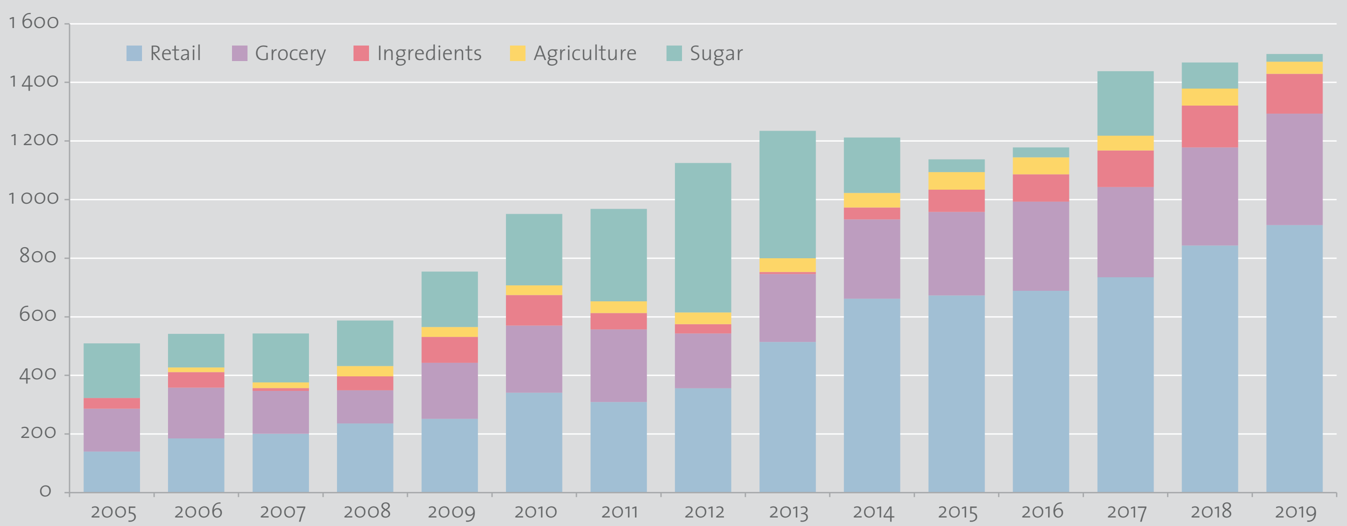
The Weston family continues to be heavily involved in ABF, with the Garfield Weston Foundation the majority shareholder and Garfield Weston's grandson, George Weston, the CEO. The group has grown organically and through acquisition to become a portfolio of cyclical businesses (sugar and agriculture) combined with more stable industries (food manufacturing, ingredients and clothing retail). We discuss the various divisions, particularly Primark, in reference to the evolution of ABF's operating profit since 2005, as *charted below*.

- **Sugar:** ABF has sugar businesses in Europe (UK and Spain), China and Africa (through its subsidiary, Illovo). Contributions to group operating profit have varied significantly over time, highlighting the cyclical nature of the commodity and the benefit the group enjoyed from the favourable EU sugar reform - phased out in September 2017. Globally, recent performance has been poor due to weak sugar prices as supply exceeded demand. However, current prices have recovered and profits in this division have somewhat normalised.
- **Grocery:** The most profitable global grocery brands in this division are the leading hot beverage brands, Twinings (tea) and Ovaltine (malt-based beverage). ABF also produces a range of cereals (Jordans and Dorset), crispbreads (Ryvita), bread (Kingsmill) and cooking sauces (Patak and Blue Dragon) in Europe. It has a sizeable edible oils and baking ingredients business in the US and Mexico, and produces a broad range of meat and bread products in Australia.
- **Ingredients:** ABF is an international leader in yeast and bakery ingredients, which are supplied to bakeries and foodservice companies worldwide. The speciality ingredients produced are value-added products such as enzymes, speciality lipids and yeast extracts (for use in food and non-food applications).
- **Agriculture:** This division produces a range of animal feed and other specialist co-products, which are supplied to farmers and food manufacturers.
- **Retail:** Primark has been an enormous success for ABF, growing its operating profit from £100 million in 2005 to over £900 million in 2019.

Primark: more for less

Primark began trading as Penney's in Ireland in the 1960s and subsequently grew in Ireland and the UK, which now comprise 58% of its 384 stores. This tremendously successful fast-fashion clothing retailer has disrupted the clothing market with its low-cost, high volume business model - much like Aldi and Lidl have done in European food retailing. Primark products can be likened to those of South Africa's Mr Price, although prices are comparatively lower and the overall shopping experience is on a far larger scale.

ABF operating profit (£m)



Source: company reports

A unique business model

Primark has struck a balance between good quality products and very affordable prices, winning the hearts and wallets of consumers. Prices are often as much as 50% cheaper than competitors due to the significant volumes of product that Primark typically sells, which results in bulk sourcing at very competitive prices. Primark is estimated to sell six times the number of items than H&M (a competing large clothing retailer) in the UK[1].

Primark's supply chain and store base is designed for large volumes and, therefore, most of its stores are huge (averaging 3 700 square meters) - usually three times the size of competitor stores - with around 55 till points available (compared to an H&M store with only five or six).

Despite selling items at a massive discount relative to its two primary listed competitors (Inditex and H&M) and having significantly larger stores, Primark's sales densities (sales per square meter of floor space) remain consistently superior, as *indicated below*. With rental and other operating expenses dictated by store size, having high sales densities is vital to boost overall store profitability.

[1] Based on Morgan Stanley estimates, on a per square foot basis.

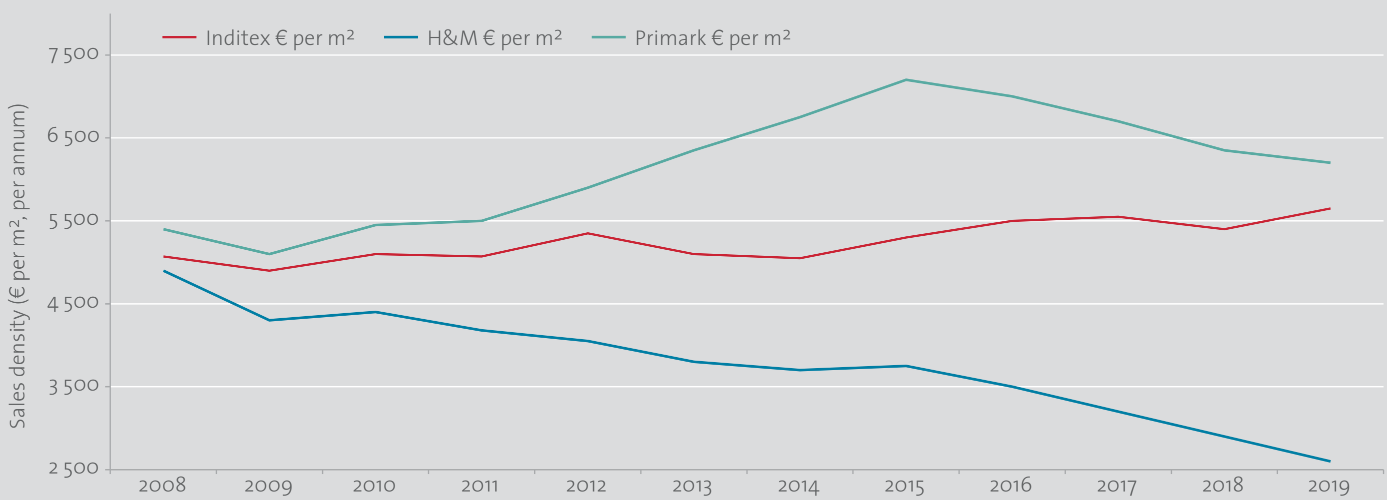
Bucking the online trends

A strategic element in Primark's business formula is that none of its products are available online, therefore customers must shop in store. A weak online offering has seen many competitors fail as consumers increasingly opt for the convenience of shopping online - a trend further bolstered by the recent COVID-19 mobility restrictions. In the UK alone, online clothing sales have increased from 6% of the market in 2005 to 26% in 2019, and yet, Primark has continued to gain overall market share in the clothing category despite a complete absence of online participation. This demonstrates the strength of the Primark brand, its value offering and the consumer store experience, which results in customers' healthy appetite to shop Primark's wide array of products in-store.

Slow and steady wins the race

As shown in the *left chart on the following page*, Primark has expanded at a steady, measured pace over the years - initially just in Ireland and the UK before entering Spain in 2006. Thereafter, the company gradually entered other Continental European countries, opening its first stores in Germany and the Netherlands in 2009. Since then, the European expansion has continued apace, with most key regions targeted. Recent successful store openings in the vast retail market of the US

Primark sales per m² vs competitors



Note: Although H&M discloses store numbers it does not disclose selling space, so the selling space data used to calculate sales densities for H&M is a Morgan Stanley estimate based on company disclosed store numbers.
Source: company data, Morgan Stanley research

ABF is back in fashion

and the high-growth Eastern European markets, suggest that Primark is at the early stages of its growth journey.

Primark has rolled out an average of 22 stores per year since 2005, underlining a conservative management strategy, despite an evidently successful, proven business model. In contrast, the aggressive store rollouts of its competitors, H&M and Inditex, have averaged 291 and 368 stores per year respectively, resulting in massive global businesses *(right chart below)*. In our view, this highlights Primark's growth opportunity, with huge potential for expansion given that the current store base is markedly lower than competitors. This is a vastly different proposition to almost all other established clothing retailers that are presently shrinking their physical store bases as footfall traffic declines due to online shopping.

Surviving the pandemic

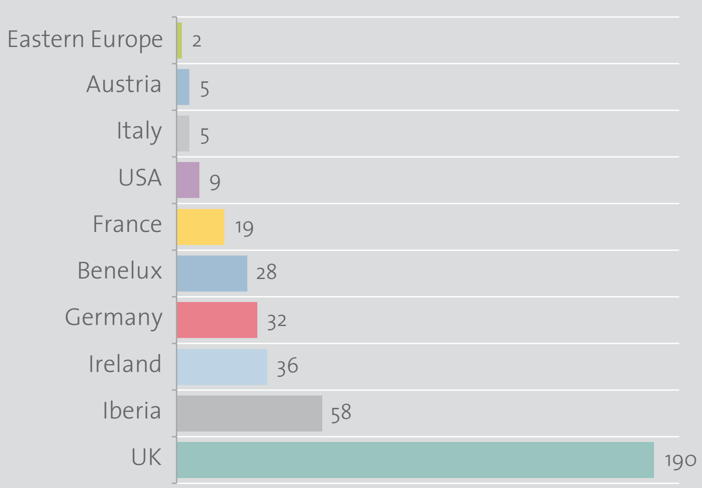
The COVID-19 pandemic and resultant hard lockdown in early 2020 placed huge strain on the revenues and cash flows of clothing retailers worldwide. While Primark was not spared, it weathered the storm by reducing cash burn to an acceptable level (mainly through furloughing staff and delaying/reducing rent) and trading at strong levels after reopening. In many ways, this has further highlighted the robustness of the business model and customer offering.

The whole attractive package

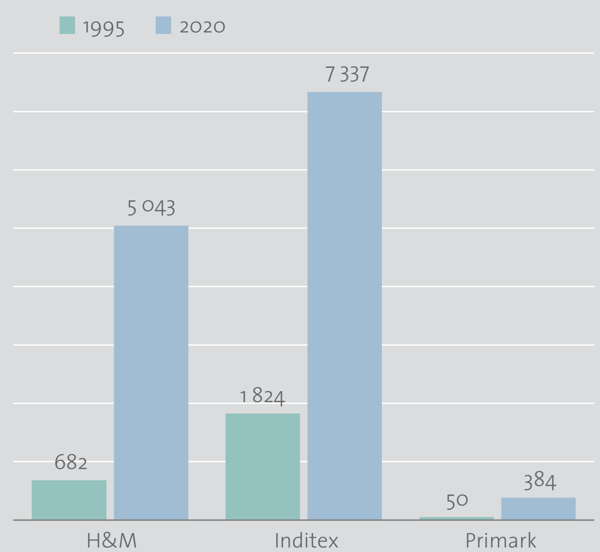
In our view, the Primark business model is very difficult to replicate due to the massive upfront scale requirements needed to compete on price. For existing retailers to compete with Primark pricing, volumes would need to be increased greatly, to the point where supply chains would not be able to cope.

Primark is undoubtedly the star of the ABF show. However, consistently good growth and returns from the other divisions over the years has resulted in these cash flows being reinvested into Primark, enabling its phenomenal growth. This recipe of sound capital allocation and measured expansion should clear the runway for future growth at ABF - one that is evidently long and bright. UP

Primark store breakdown by geography



Store growth (1995 - 2020)



Source: company reports

Kagiso Asset Management Funds

Performance to 31 December 2020	1 year	3 years[1]	5 years[1]	10 years[1]	Since launch[1]	Launch	TER[2]	TC[3]
Unit trust funds[4]								
Equity Alpha Fund	3.5%	6.8%	9.5%	9.2%	15.6%	Apr-04	2.11%	0.51%
SA Equity General funds mean	2.2%	0.1%	3.0%	6.9%	11.6%			
Outperformance	1.3%	6.7%	6.5%	2.3%	4.0%			
Global Equity Feeder Fund#	6.0	-	-	-	5.5%	Nov-19	3.20%	0.34%
Global Equity general funds mean	20.3				15.6%			
Outperformance	-14.3				-10.1%			
Balanced Fund	2.2%	6.0%	8.5%	-	8.7%	May-11	1.62%	0.43%
SA Multi Asset High Equity funds mean	5.2%	3.5%	4.4%		7.8%			
Outperformance	-3.0%	2.5%	4.1%		0.9%			
Protector Fund	1.8%	6.7%	8.3%	6.7%	9.5%	Dec-02	1.60%	0.36%
CPI + 4%	6.8%	7.9%	9.0%	9.8%	10.2%			
Outperformance	-5.0%	-1.2%	-0.7%	-3.1%	-0.7%			
Stable Fund	-3.9%	5.2%	7.5%	-	7.3%	May-11	1.53%	0.46%
Total return of CPI + 2% pa	4.9%	5.8%	6.0%		5.7%			
Outperformance	-8.8%	-0.6%	1.5%		1.6%			
Institutional funds[5]								
Managed Equity Fund (SWIX)*	1.6%	5.7%	8.7%	8.9%	11.0%	Sep-06		
FTSE/JSE SWIX All Share Index	0.6%	-1.1%	4.1%	9.0%	10.3%			
Outperformance	1.0%	6.8%	4.6%	-0.1%	0.7%			
Domestic Balanced Fund[6]	1.7%	6.6%	9.6%	8.0%	8.4%	May-07		
Peer median	1.3%	1.4%	5.2%	8.1%	8.2%			
Outperformance	0.4%	5.2%	4.4%	-0.1%	0.2%			
Global Balanced Fund[7]	3.7%	7.7%	9.8%	-	9.3%	Jul-13		
Peer median	5.4%	4.7%	5.7%		8.4%			
Outperformance	-1.7%	3.0%	4.1%		1.0%			
Bond Fund	7.0%	8.9%	10.8%	-	8.8%	Aug-15		
BESA All Bond Index	8.6%	8.9%	10.4%		8.3%			
Outperformance	-1.7%	0.0%	0.4%		0.5%			
Money Market Fund	6.6%	7.8%	8.1%	7.1%	7.8%	Jan-04		
Alexander Forbes STeFI Composite Index	5.4%	6.6%	7.0%	6.4%	7.2%			
Outperformance	1.2%	1.2%	1.1%	0.7%	0.6%			
Sharia unit trust funds[4]								
Islamic Equity Fund	5.2%	5.8%	9.1%	7.8%	10.4%	Jul-09	1.54%	0.23%
SA Equity General funds mean	2.2%	0.1%	3.0%	6.9%	9.3%			
Outperformance	3.0%	5.7%	6.1%	0.9%	1.1%			
Islamic Global Equity Feeder Fund#	8.9%	-	-	-	11.8%	Jan-19	2.81%	0.18%
Global Equity General funds mean	20.3%				22.0%			
Outperformance	-11.4%				-10.2%			
Islamic Balanced Fund	8.2%	6.3%	7.7%	-	7.0%	May-11	1.55%	0.17%
SA Multi Asset High Equity funds mean	5.2%	3.5%	4.4%		7.8%			
Outperformance	3.0%	2.8%	3.3%		-0.8%			
Islamic High Yield Fund#	6.4%	-	-	-	6.5%	Mar-19	0.57%	0.07%
Short-term Fixed Interest Index (STeFI)	5.4%				6.3%			
Outperformance	1.0%				0.2%			

Highest and lowest monthly fund performance	Highest	Lowest	Highest	Lowest	Highest	Lowest	Highest	Lowest	Highest	Lowest
Equity Alpha Fund	12.6%	-21.6%	12.6%	-21.6%	12.6%	-21.6%	12.6%	-21.6%	12.6%	-21.6%
Balanced Fund	9.1%	-15.7%	9.1%	-15.7%	9.1%	-15.7%	-	-	9.1%	-15.7%
Protector Fund	7.4%	-13.9%	7.4%	-13.9%	7.4%	-13.9%	7.4%	-13.9%	9.5%	-13.9%
Stable Fund	6.1%	-11.4%	6.1%	-11.4%	6.1%	-11.4%	-	-	6.1%	-11.4%
Islamic Equity Fund	9.6%	-14.3%	9.6%	-14.3%	9.6%	-14.3%	9.6%	-14.3%	9.6%	-14.3%
Islamic Balanced Fund	8.0%	-9.3%	8.0%	-9.3%	8.0%	-9.3%	-	-	8.2%	-9.3%

Footnote and disclaimer follow overleaf.

Kagiso Asset Management (Pty) Limited

Fifth Floor MontClare Place
Cnr Campground and Main Roads
Claremont 7708

PO Box 1016 Cape Town 8000

Tel +27 21 673 6300 Fax +27 86 675 8501

Email info@kagisoam.com

Website www.kagisoam.com

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Footnote: [1] Annualised (ie the average annual return over the given time period); [2] TER (total expense ratio) = % of average NAV of portfolio incurred as charges, levies and fees in the management of the portfolio for the rolling three-year period to 31 December 2020; [3] Transaction costs (TC) are unavoidable costs incurred in administering the financial products offered by Kagiso Collective Investments and impact financial product returns. It 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. This is also calculated on the rolling three-year period to 31 December 2020; # over 12 months to 31 December 2020.

[4] Source: Morningstar; net of all costs incurred within the fund and measured using NAV prices with income distributions reinvested; [5] Source: Kagiso Asset Management; gross of management fees; [6] Median return of Alexander Forbes SA Manager Watch: BIV Survey; [7] Median return of Alexander Forbes Global Large Manager Watch.

* Our two Managed Equity composites have been amalgamated with immediate effect. The history of Managed Equity (SWIX) has been maintained and the benchmark changed to Capped SWIX with effect from 1 July 2019. In future, therefore, we have just one Managed Equity composite with a Capped SWIX benchmark. This change has been implemented after consultation with our GIPS auditors, and therefore our composites will continue to be GIPS verified going forward.