Capricorn Unit Trusts' Annual Financial Statements

The summarised report of the 30 June 2021 Annual Financial Statements of all the Capricorn Unit Trust Funds are available on our website under the "News Platform" section. View it here now: Financial Statements.

The audited Financial Statements and the auditor's report thereon are available for inspection at the company's registered office.

Investment lessons to be learnt from the Covid-19 pandemic

Although the pandemic is by no means over, there are valuable lessons that investors can learn from the past year.

Winston Churchill once said, "Never let a good crisis go to waste," and that's precisely the mindset investors should have in times like these. Bryant McGill said, "Suffering is one of life's great teachers", very true but it's unfortunate that some lessons can only be learned in times of hardship. When we look at how markets worldwide have suffered and in many places are still suffering, we rightly say the Covid-19 pandemic qualifies as a learning moment in time.

Many seasoned and disciplined investors' investment portfolios were properly positioned for the pandemic and their actions during the pandemic were admirable. But there were also investors whose portfolios were in no way prepared for the pandemic and worse, whose decisions during the pandemic caused severe damage to their portfolios.

The primary lessons one can and perhaps should take from the pandemic are:

- **Expect the unexpected.** Covid-19 has taught us that a storm can arise without any prior warnings and cause severe damage if you are not prepared. So, make sure your portfolio is ready for storms, ask the tough questions, do a "what if" analysis, and see if your investment portfolio can withstand these stress tests. What does a portfolio look like that's ready for storms? Firstly, it is structured to provide for unforeseen events and has enough liquidity to withstand a crisis. Usually, the feeling was that 3-6 months of expenditure is sufficient, but Covid-19 has taught us that you need to be prepared for much longer. Also make sure a healthy part of your portfolio is liquid so that when you need to convert it into cash, you can do it quickly and without realising capital losses in the process. Another absolute necessity of a portfolio that can survive a crisis is a well-diversified portfolio. Don't have all your eggs in one basket, spread things out between different asset classes, other currencies and make sure you get proper advice on this before you tackle it.
- **Beware of your own emotions.** In times of crisis, investors' emotions are usually their biggest enemy and sometimes result in panicked decisions which cause far more damage to their finances than the market situation does. So, stay calm, get proper advice from experienced investment experts before making any distressed leaps.
- **Make it very clear to yourself what your investment strategy is.** When you're sure where you're going and how you plan to get there, times of crisis are unlikely to stop you. When we talk about investments, it's usually about the long term, so keep focusing on the long-term and beware of those short-term fluctuations that make you relinquish your long-term plan.
- **Invest Sensibly.** Our investment philosophy has stood the test of Covid-19. Always diversify, never speculate, keep it simple, continuously monitor and evaluate actual performance, see every investment opportunity as unique thus warranting a distinctive approach, fully understand the characteristics of an investment and clearly define and quantify all risk factors associated with an investment.
- **Be ready to seize opportunities.** Some industries have been permanently affected by Covid-19. One may need to avoid some industries, but there are opportunities in other industries that look innovative and promising. With our indexing strategy we have seen value by passively tracking the benchmark indexes which delivers consistent performance.

These are a few lessons we can take with us to achieve investment success.

Economic Update

Evergrande. Up to a week ago one might be forgiven for not having heard of it. But suddenly, the debt-laden Chinese property company is at the forefront of investors' worries. Its U$300bn balance sheet makes it the second-largest property development investment and -management company in China. It is still solvent, just. But it has run into a liquidity crunch.

Evergrande is the latest victim of the CCP's urge to tighten regulation over a vast swathe of the Chinese economy ranging from education to internet and gambling industries as well as property. The CCP laid down "three red lines" concerning a firm's balance sheet which must be complied with before it can borrow more. Evergrande was found to be too geared already and could not borrow more to obtain liquidity.

We believe creditors of Evergrande will rank as follows (1) citizens that made down payments or pre-paid for properties (2) vendors and suppliers (3) onshore bondholders (4) offshore bondholders and (5) shareholders. Of these, the obligations on pre-paid properties are the largest. It is likely to default on its offshore debt, estimated to amount to U$15bn. It is not a Lehman moment, because Evergrande is not at the centre of the global financial system like Lehman and Bear Stearns were in the Great Credit Crisis of 2008/9. It remains to be seen whether the CCP will regard it as too-big-to-fail in the Chinese financial system. It certainly has the potential to hurt the banks.

At the time of writing, Evergrande remains unresolved. However, we think the longer term, structural implications are already apparent. There will be a substantial cooling of the Chinese property sector and therefore, the economy. After the surge in 2021, it is likely to slow to around or just below 5%. With China consuming roughly 50% of all commodity production, this means that the bull market in commodities will fade, having an adverse effect on economies that produce them.

We think a key result for us as investors will be a weaker rand. It will not crash or "blow out" as we saw at the outset of Covid-19. However, the strong tailwinds that have driven the rand from 19.00 to 14.00 per dollar, will fade. These were, largely, the surge in commodities and big balance of payments surpluses. However, the continued, significantly positive, interest rate differential will support the rand and prevent a "blow out".

The best protection against these market risks is diversification. This means that one should maintain exposure to a variety of asset classes in order the achieve growth in wealth. Given our currency view, in our diversified multi-asset funds, we maintain an overweight exposure to offshore equity via our International Fund. The Fund invests in Developed Markets only with its largest holdings in the USA. It is therefore not directly exposed to emerging markets such as China. The International Fund returned 16.9% year-to-date to August.

Furthermore, we maintain that domestic bonds, that is Namibian and South African, carry an attractive yield for these uncertain times. Namibian inflation linked bonds are also very attractively priced and protect the investor against the danger of future inflation. Therefore, we are fully invested in these. The key factor to watch is counterparty risk, that is fiscal prospects of these Governments. The Bond Fund returned 16.7% for the 12 months to August.

Our domestic equity exposure is limited to the Top 40 JSE shares in the form of a capped index. This means that very large-cap companies like Naspers are limited to a weight of 10%. As for the rest, it is a well-diversified and, now cheap, portfolio of shares containing, amongst others, banks, insurers, retail, telecoms, platinum, gold, diversified miners, Sasol as well as industrial rand hedges like Richemont, British American Tobacco and AB InBev. The Equity fund returned 25.8% for the twelve months to August.