CONTRARIUS

# QUARTERLY INVESTOR COMMENTARY
## 30 JUNE 2012

## CONTRARIUS GLOBAL EQUITY FUND

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*The Fund aims to earn a higher Total Rate of Return than the average of the world's equity markets, as represented by the MSCI World Index, including the reinvestment of dividends net of withholding tax ("World Index"). It aims to achieve this without greater risk of loss, over the long-term. The Fund is an actively managed fund, and as such does not in any way seek to replicate its benchmark index, but may instead differ materially from the performance benchmark in order to achieve its objective.*

**CONTRARIUS GLOBAL EQUITY FUND AT 30 JUNE 2012**

| Total Rate of Return in US Dollars | Class | Since Inception on 1 Jan 2009 | Latest 3 Years | Latest 1 Year | 2012 Year-to-date | Latest Quarter |
|---|---|---|---|---|---|---|
| | | *% Annualised* | | | *% Not Annualised* | |
| **Contrarius Global Equity** | **Investor** | **25.3** | **17.5** | **(3.6)** | **4.6** | **(7.2)** |
| **Contrarius Global Equity** | **Institutional** | **25.8** | **18.0** | **(3.2)** | **4.8** | **(7.1)** |
| World Index | | 11.3 | 11.0 | (5.0) | 5.9 | (5.1) |

The Fund's Investor Class shares returned (7.2)% for the quarter versus (5.1)% for the benchmark MSCI World Index, including reinvested net income. As we have highlighted previously, our investment philosophy is not benchmark cognisant and our portfolios would normally vary materially from the benchmark World Index. The Fund's returns are therefore likely to deviate from those of the benchmark. Investors are reminded that given the long-term, contrarian, valuation-based investment philosophy, there will be times when the Fund will materially underperform its benchmark in the short-term in order to achieve its objective of long-term outperformance.

The Fund remains significantly overweight Technology (particularly US Technology) and Consumer Discretionary stocks. In terms of geographic exposure, the Fund continues to be significantly overweight US equities. While the Fund continues to be underweight European equities it has increased its exposure from 6% to 14% over the quarter. The extended period of underperformance of European equities has resulted in certain intriguing investment opportunities.

| Sector Exposure 30 Jun 2012 | Weighting (%) Fund | World Index [1] | Over/(Under) Weight |
|---|---|---|---|
| Energy | 0 | 11 | (11) |
| Materials | 1 | 7 | (6) |
| Industrials | 1 | 11 | (10) |
| Consumer Discretionary | 31 | 11 | 21 |
| Consumer Staples | 6 | 11 | (5) |
| Health Care | 1 | 11 | (10) |
| Financials | 7 | 19 | (12) |
| Information Technology | 48 | 13 | 35 |
| Telecommunication Services | 3 | 4 | (1) |
| Utilities | 0 | 4 | (4) |
| **Total Shares** | **98** | **100** | |
| Net Current Assets | 2 | - | |
| **Net Assets** | **100** | **100** | |

[1] *Source: MSCI (attention is drawn to MSCI disclaimer in 'Notices')*

| Geographic Exposure 30 Jun 2012 | Weighting (%) Fund | World Index [1] | Over/(Under) Weight |
|---|---|---|---|
| North America | 75 | 59 | 16 |
| Europe | 14 | 26 | (13) |
| Japan | 8 | 9 | (1) |
| Other | 2 | 6 | (4) |
| **Total Shares** | 98 | **100** | |
| Net Current Assets | 2 | - | |
| **Net Assets** | **100** | **100** | |

[1] *Source: MSCI (attention is drawn to MSCI disclaimer in 'Notices')*

As indicated above, 48% of the Fund is invested in Technology shares. They account for seven out of the Fund's top ten holdings. This is not because we have any particular view on the sector but rather a result of contrarian bottom-up stock picking, which continues to yield unusually attractive investment opportunities within Technology. This can be seen in the breadth of these investments, spanning software, consumer technology, networking, internet services and semiconductors. Consider, for example, NVIDIA and Oracle.

**NVIDIA**

Until a few years ago, NVIDIA operated almost exclusively in the somewhat esoteric niche of graphics processing units (GPUs). At the core of any computer is the central processing unit (CPU)—a general-purpose microprocessor that coordinates and carries out most of the work. In the early days of computing, the CPU executed essentially all the instructions, and did so one at a time. Manipulating an image could require hundreds of thousands or even millions of instructions, which was a burden on the CPU. But graphics-related tasks tend to fall into a relatively small set of geometric and mathematical operations (for example, rotation, resizing, perspective, lighting, shading) and in 1983 Intel introduced a separate piece of hardware designed to handle only these, freeing up the CPU. By the early 2000s, the market for high-end graphics hardware was almost entirely won by NVIDIA and ATI, with Intel being the leader in less powerful graphics processors that were integrated with its CPUs. In 2006, AMD, which is Intel's primary competitor, bought ATI.

It turned out that a number of the things that make a GPU useful (including the ability to carry out many instructions simultaneously and their handling of certain branches of mathematics) have many non-graphical applications. The expanding scope of GPUs began to encroach on CPUs. Whereas Intel started with the CPU and eventually integrated graphics processors, NVIDIA started with the GPU and eventually developed general processors. Today, NVIDIA chips power devices ranging from mobile phones and tablets to some of the world's fastest supercomputers.

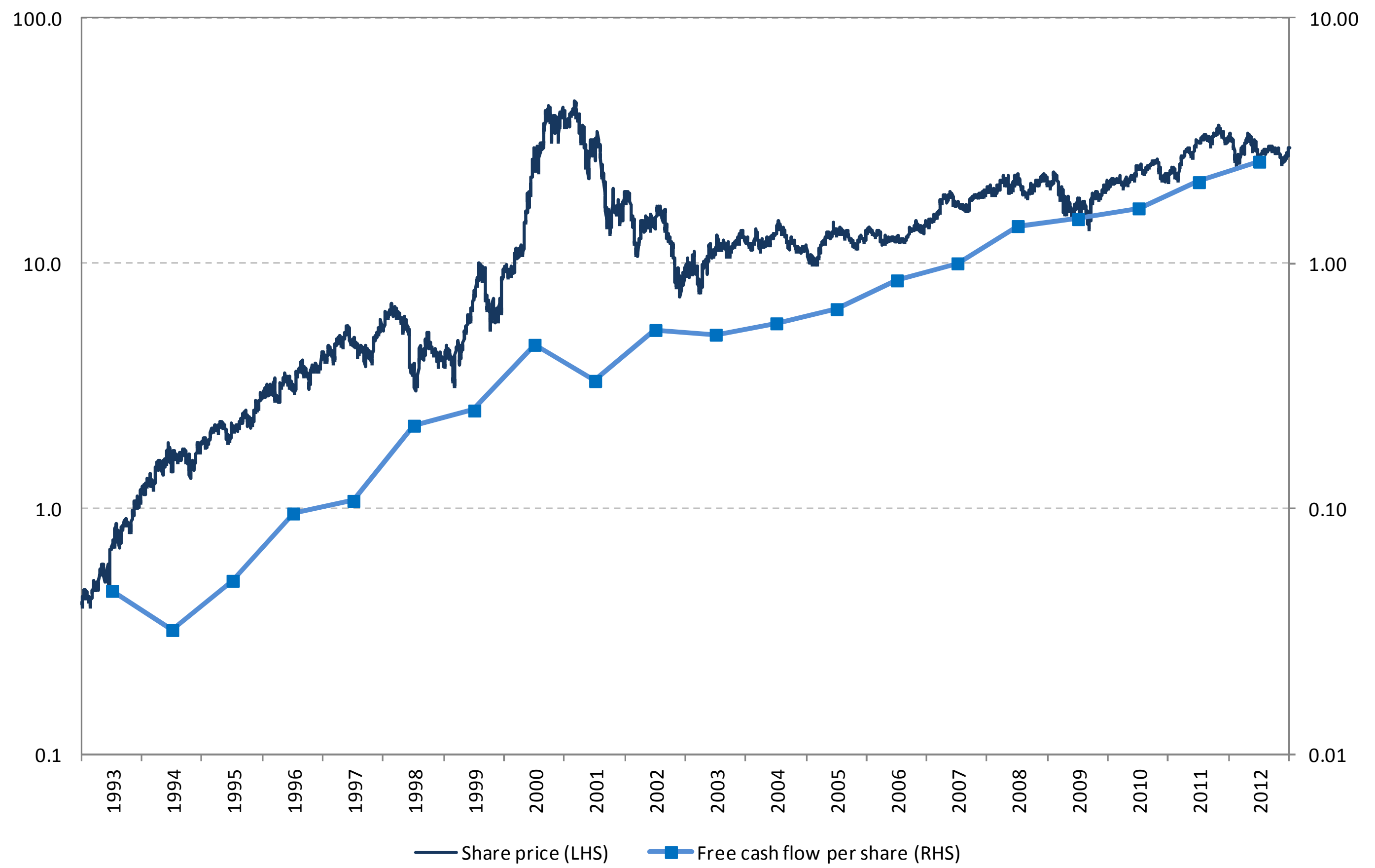
In 2011, shipments of smart phones and tablet computers grew 74% to 560 million units. In comparison, PC shipments increased 2% to 352 million units. Mobile processors appear to be a very promising opportunity even though they currently make only a relatively small contribution to NVIDIA's revenues. The recently announced Google Nexus 7 and Microsoft Surface (Windows RT model) tablets both include NVIDIA processors. We therefore find it somewhat surprising, given the significant growth opportunities, that adjusting for net cash NVIDIA trades on approximately 9x historic annual free cash flow.

**ORACLE**

Although Oracle may be a less familiar name than some of the Fund's other Technology holdings, its products are no less a part of everyday life. Oracle is the leading vendor of database management systems, which make it possible to store and analyse large amounts of information. The business was founded in 1977 based on an IBM paper describing the database system that IBM had invented and was developing. Oracle beat IBM to market. It was much loved during the 1990s and the share price increased by more than 100x from 1992 to 2000, leaving it valued at nearly a hundred times free cash flow. The share subsequently fell more than 80%.

Figure 1 shows free cash flow per share compared to the share price over the past two decades. Oracle's history of innovation and astute decision making is evident in the ongoing growth of free cash flow per share. Unusually for Technology businesses, Oracle's operating profit margins *increased* during the bursting of the Technology, Media and Telecom bubble of 1999-2000 and have remained at similar levels (even after buying Sun Microsystems, to a large extent a lower-margin hardware business, in early 2010). Despite its good long-term growth prospects, adjusting for net cash, Oracle sells for approximately 10x historic free cash flow.

**Figure 1: Oracle**




*Semi-log chart*
*Source: Contrarius Research, Bloomberg*

### Comparison with Integrated Energy Companies

NVIDIA and Oracle are clearly very different businesses. However, we believe that they share a number of characteristics, such as strong positions in their industries, solid balance sheets and excellent free cash flow generation. The last is particularly interesting when compared to some other companies with apparently low valuations, such as the large integrated energy businesses, in which the Fund has no holdings. Figure 2 shows the top five members of the MSCI World Energy Index compared to NVIDIA, Oracle and the Fund's three largest Technology holdings (Apple, Cisco and Microsoft). Energy producers tend to require considerable ongoing capital investment, in part to replace depleted resources and to maintain their reserve lives. As a result, their free cash flow (FCF) is typically well below their accounting profits. Simple valuation metrics, such as the price-to-earnings (PE) ratio, may therefore not be appropriate in determining their attractiveness as investments.

| **Figure 2**<br>**Free Cash Flow versus Earnings** | **FCF vs Earnings** | **PE Ratio** | **Enterprise Value to FCF** |
|---|---|---|---|
| **Energy Companies** | | | |
| Exxon Mobil | 65% | 10.0 | 13.9 |
| Chevron | 34% | 7.7 | 18.9 |
| BP | 15% | 5.3 | 36.3 |
| Royal Dutch Shell | 37% | 7.1 | 16.7 |
| Total | 11% | 9.0 | 86.7 |
| **Technology Companies** | | | |
| NVIDIA | 117% | 16.9 | 9.2 |
| Oracle | 131% | 14.5 | 10.0 |
| Apple | 124% | 14.1 | 9.1 |
| Cisco Systems | 138% | 12.5 | 5.2 |
| Microsoft | 118% | 11.0 | 7.3 |

*Enterprise value is as of 30 June 2012. Earnings and free cash flow are for the trailing twelve months. FCF is not adjusted for interest.*

*Source: Contrarius Research, MSCI, Bloomberg*

For all five of the Energy companies, free cash flow is weaker than earnings while the opposite is true of all five of the Technology companies. These differences are highlighted in figure 3 where we look more closely at the top two members of the MSCI World Index: Apple and Exxon Mobil.

| **Figure 3**<br>**Exxon Mobil versus Apple (USD'bn)** | **Exxon Mobil** | **Apple** |
|---|---|---|
| Market Capitalisation | 400 | 546 |
| Less: Net Cash and Investments | (38) | (110) |
| Enterprise Value | 363 | 436 |
| Capital Expenditure | 32 | 5 |
| Earnings | 40 | 39 |
| Free Cash Flow | 26 | 48 |
| PE Ratio | 10.0x | 14.1x |
| Enterprise Value to FCF | 13.9x | 9.1x |

*Enterprise value is as of 30 June 2012. Other numbers are for the trailing twelve months. FCF is not adjusted for interest.*

*Source: Contrarius Research, MSCI, Bloomberg*

The theme common to a number of the Fund's Technology holdings, including NVIDIA and Oracle, is that we believe that they are high quality, growing businesses with relatively low capital requirements. This should result in strong and growing cash generation, which is expected to accrue to shareholders over time.

### Conclusion

As is often the case, many risks present in global financial markets remain unresolved, which, depending on how they develop, may impact asset prices and resultant returns to investors. Whilst mindful of these risks, our focus continues to be on bottom-up fundamental analysis to find companies that we believe offer the prospect of attractive long-term returns.

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