Naspers’ most notable investment is Prosus, which in turn has a large shareholding (31%) in Chinese internet giant Tencent. Prosus is focused on e-Commerce, Food Delivery, and Classifieds. While classifieds and even food delivery will be impacted during the Covid-19 outbreak, its other digital assets may see improved adoption and continued growth during this time.

- Tencent released FY19 results earlier this month in which it showed strong earnings and revenue growth. Tencent is mainly China-based, which means it was impacted by Covid-19 by the time it delivered results. At the time, management said that its payments business took a hit but that it had already recovered by mid-March.
- Tencent has seen a significant improvement in user engagement, especially in new areas such as Tencent Work and Tencent Meetings. Mini-program user engagement in apps such as Healthcare also did well.
- The Covid-19 outbreak has hastened the speed of digitalisation among users. This should be an important step forward for the tech sector overall.
- Naspers has a high cash balance and is able to buy back shares to assist in narrowing the discount it trades at relative to Prosus.

The discount that both Naspers and Prosus trade at relative to Tencent has widened recently (in the sell-off). We continue to like the sector and believe there is significant upside to both the Naspers and Prosus share price.

British American Tobacco (BTI)

British American Tobacco remains one of the most defensive companies globally and we believe it will be able better able to weather high volatility in the market and the impacts of the Covid-19 outbreak. By way of an example, Italian cigarette sales grew 2% in January and only slowed to 0% in February, which illustrates the low volatility of its main profit drivers. Management added that even though there has been a limited impact on turnover, it will be seeking £1 billion in additional cost savings over the next three years to offset the impact of Covid-19. This constitutes ~9% of profit and will result in the operating margin expanding by 380 basis points by year three (all else being equal). Additionally:

- The business has gained market share in cigarettes every year for the past seven to eight years. Given strong pricing power and cost control, the business has been able to consistently expand margins and deliver high–single–digit earnings growth. This provides good visibility of earnings against an increasingly murky global growth outlook.
- British American Tobacco is highly cash flow generative resulting in good dividend flows and we expect gearing levels (net debt/EBITDA) to drop below 3 times next year, further lowering risk.
- In addition, the company is the number one player in vapour and oral tobacco globally and has strongly grown its Next Generation Products (NGP) portfolio. At recent Capital Market Days, management said it aims to increase NGP customers five-fold by 2030 to 50 million customers (currently 11 million) in a deliberate tilt to healthier alternatives.
- The US regulatory landscape has improved, which underpinned a re-rating of the stock before the market sell-off. While regulation remains a key risk, higher regulation increases barriers to entry making it much more difficult for independents to gain market share.
British American Tobacco’s share price has come under pressure during the current market sell-off and we view the current price as an attractive entry point into the stock.

Bidvest (BVT)

Bidvest is a diversified industrial company and thus not immune to the domestic South African economic weakness. However, its diversified nature and growth opportunities make it our preferred company within the sector.

- The company is not highly geared and will probably use the current environment to make smaller bolt-on acquisitions at good prices.
- Although some of its smaller contributors will struggle in the current environment, the services division – which incorporates Steiner (hygiene services) – should do well during this time. Services currently contribute 29% to trading profit and this will increase once the PHS transaction concludes by June 2020. PHS is a hygiene services business in the UK, Ireland and Spain and should do well, especially subsequent to the current virus outbreak. This transaction is immediately earnings accretive (+7% per management but will be more so at the current weak rand exchange rate).
- The company’s new LPG terminal in Richards Bay should come online by June and the freight division is expecting to do better because of a better maize harvest.
- Despite the difficult trading conditions, the company managed to grow trading margins in the first half to December 2019 by keeping like-for-like costs growth to 2.7%.

Because of new acquisitions and additions to its businesses, Bidvest should show earnings growth in FY21 north of 15%. We view the stock as offering reasonable upside from current levels and we expect the dividend to be maintained, adding a further 4.1% to the expected return.

Spar (SPP)

Spar’s business will be relatively resilient during the Covid-19 outbreak and it should exhibit low profit volatility compared to its retail and industrial peers. Historically food sales have not declined even during the harsh recessions experienced in 1992, 1999 and 2009, and thus the business offers both growth and defensiveness in these uncertain and volatile markets.
Furthermore:

- Spar has consistently been one of the highest quality companies in the South African market due to its high return on invested capital and dividend growth coupled with high free cash flow growth.
- The business model is defensive since it is mainly a food retailer and has low volatility in margins since it is focused more on distribution/wholesaling.
- The business is well run with a strong track record of growing sales faster than peers. It also has a strong balance sheet. This business offers defensive upside from current levels, coupled with a dividend yield of 4.6%, which is attractive as many retailers are likely to cut dividends or pay no dividends during this period.

**Sanlam (SLM)**

Sanlam is our pick in the financial sector currently. The company has de-rated significantly during the recent global markets sell-off and it now trades at a substantial discount to its embedded value.

- Earnings are defensive relative to peers due to geographic and product diversification. Its recent expansion into Morocco is also an exciting growth prospect.
- Exposure to different market segments, with entry level markets offering higher growth prospects and wider margins.
- Sanlam holds a majority stake in Santam – a market leader in short-term insurance.
- The company is adequately capitalised. In an update to the market earlier this week, it said that Sanlam Life’s Solvency Capital Requirement (SCR) cover ratio was 188% on 25 March. The company targets a SCR cover ratio of 170% to 210%. At the lower end of this range (170%), Sanlam Life can withstand at least two economic shocks without breaching the minimum SCR cover ratio of 100%.
- Sanlam has a solid and deep management team with a strong track record. And the company has a history of conservative and transparent accounting treatment.

Sanlam is trading at a discount to EV of 23.3%, which has expanded significantly since the full-year mark (FY19: discount of 7.5%). The company has historically traded at a premium to its embedded value due to its superior margins and relatively higher growth prospects.
BHP Group (BHP)

BHP Group (BHP) continues to operate quality assets that are highly cash generative even at low commodity prices, given their relatively low cash production costs.

- The company has a strong balance sheet, with net-debt to EBITDA below 0.5 times, which we view as insurance during periods of market distress.
- Solid cash generation coupled with low Capex commitment will enable the company to continue paying attractive dividends throughout our forecast period.
- Well diversified from a geographic and commodity perspective. Assets are mostly long life and in low- to moderate risk countries.
- The company boasts best-in-class capital allocation.

The share trades on an 8.0 times forward PE against its long-term average of 11.5 times. It also offers a forward dividend yield of 8.0% and a free cash flow yield of 12.1%, which we view as attractive.