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Whether Naspers can solve what appears to be a structural issue is questionable

It is evident that whatever the strategy of Bob van Dyk it is not delivering the expected outcomes to investors

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11 FEBRUARY 2021 - 13:16 *by* JARRED HOUSTON

A logo of Tencent is seen at its booth at the 2020 China International Fair for Trade in Services in Beijing, China. Picture: REUTERS/TINGSHU WANG

Koos Bekker's decision to buy a 46.5% stake in Tencent in 2001 for \$32m will go down as one of the best investments of all time and one that has single-handedly changed the landscape of the SA investment industry.

The company has evolved from a little-known messaging platform to one of the largest technology companies in the world with a business that has interests in just about every part of the internet ecosystem in China as well as global interests through gaming, media and its nearly \$300bn investee portfolio.

With the enormous rise in value of Tencent, Naspers has come to dominate the JSE all share index, with the combined weighting of Naspers and Prosus now accounting for more than a 20% of the index. This is in spite of the fact that Naspers trades at a near 50% discount to the see-through value of its stake in Tencent alone and a discount approaching 55% when including the other listed and unlisted investments in the group.

It is not unusual for holding companies to trade at large discounts to the value of their underlying investments. Some of the common reasons include costs incurred by an investment holding company; illiquidity; poor disclosure related to investments; poor capital allocation; substandard corporate governance and potential tax liabilities.

Naspers has the added factors of its N share control voting structure. The unusually large index weighting on the JSE also can force local investment managers to sell the share above a certain threshold weighting either due to mandate limits or concentration risk.

Several steps have been taken by the group to address the widening discount and it has become a matter that dominates investor meetings and management's time. The Prosus listing up to this point appears to have been wholly ineffective and has simply created a complex and costly structure. What is particularly disappointing is that this has come at the same time as we have seen a boom in listed valuations for internet companies involved in the very same space that the group's unlisted businesses play in. While the current $5bn buyback programme has been value-accretive, with the rising Tencent price, it too has done little to address the actual discount.

Perhaps investors are becoming increasingly concerned about capital allocation and the ability of Bob van Dyk and the rest of the current executives to justify their eye-watering remuneration, especially since any recent added value has been contributed almost solely by Tencent. The company was involved in highly publicised bids for Just Eat and eBay's online classifieds business but ultimately ended up losing out on both deals.

In 2020, Allegro, a Polish classifieds business that Naspers sold to private equity in 2016 for $3.2bn, had a value of $11.2bn at its initial public offering (IPO) and is currently valued at more than $19bn. Similar concerns could be raised about the 2018 sale of 2% of the Tencent stake at HK$405 per share as compared to the current price HK$762. Only time will tell whether the proceeds from these realisations deployed into other areas are able to deliver value. But it is evident that whatever the strategy of Bob van Dijk, it is not delivering the expected outcomes to investors.

We fully expect further incremental steps to be taken by the management team to address the discount but question whether they will be successful at solving what appears to be a structural problem. With SA's government seemingly at the edge of a fiscal cliff and needing to fund a vaccine programme, perhaps now is the time to consider a more permanent solution with the Tencent stake and negotiate a compromise with regard to any tax consequences.

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