DESERT LION
— CAPITAL —

OVERVIEW

DECEMBER 2023

Strategy – South African listed equities

Unlevered. Long-only.
Concentrated portfolio, 10 to 15 high conviction holdings.
Value-oriented.
Fundamental, research-driven process.
Bottom-up, with an awareness of macro factors.
Benchmark agnostic.

Portfolio Manager – Rudi van Niekerk

South African native with local, on the ground presence & knowledge.
A decade of same strategy experience investing in South African public equities.
Prior experience includes private equity & commodity trading.

Alignment

Meaningful investment from Portfolio Manager and Founders
Portfolio Manager reinvests majority of profits

Performance

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YEAR TO DATE		
													Desert Lion [1]	FTSE/JSE ALSI [2]	Delta
2019				1.4%	- 1.2%	2.9%	- 0.9%	- 10.7%	0.8%	6.1%	3.3%	3.9%	4.8%	4.7%	0.1%
2020	- 7.7%	- 14.4%	- 25.8%	2.0%	3.5%	6.9%	3.4%	5.6%	10.3%	13.2%	9.6%	12.5%	11.2%	- 1.0%	12.2%
2021	10.9%	- 2.4%	6.9%	- 2.5%	2.7%	- 2.1%	- 1.2%	- 3.3%	- 5.7%	5.9%	- 4.6%	6.1%	9.6%	14.6%	- 5.0%
2022	0.4%	- 0.0%	2.0%	- 7.3%	- 6.0%	- 7.1%	1.6%	- 0.8%	- 3.6%	- 3.5%	14.8%	0.4%	- 10.5%	- 7.3%	- 3.2%
2023	0.5%	- 7.9%	4.1%	- 0.3%	- 9.2%	5.6%	7.8%	- 5.5%	- 4.5%	- 0.7%	1.1%	4.3%	- 6.1%	- 2.1%	- 4.0%
Cumulative – inception to date [3]													7.3%	7.9%	- 0.6%
Annualized – inception to date [3]													1.5%	1.6%	- 0.1%

Fund Terms

Min subscription	$250,000
Management fee	0.75%
Performance fee	25% of profits exceeding hard hurdle
Hurdle	6% hard, non-compounding
High water mark	Yes
Soft lock-up	3 years
Early withdrawal	5%
Fund expenses	Capped at 0.5%
Withdrawals	Quarterly, 90 days notice

Notes to Performance

1. Performance represents the Fund's Standard Class and is representative of an annual management fee of 0.75%; fund expenses of 0.5% p.a.; 6% non-compounding hurdle; performance fee of 25% of profits exceeding the 6% hard hurdle; high water mark applies.
2. FTSE/JSE All Share Index ("ALSH" or "J203") converted to USD returns.
3. Net results to a Limited Partner in the Standard Class as of April 1, 2019 inception. Individual returns will vary by class and date of investment.

PAST PERFORMANCE IS NOT A GUARANTEE OF FUTURE RESULTS.

Top 6 Holdings (alphabetically)

Argent Industrial	Cash (16%)
Calgro M3	Karooooo
Sibanye Stillwater	Stadio

Top 6 concentration 67%

General Information

Fund Domicile	U.S. (Delaware)
Inception	April 2019
AUM	US$ 10m
Introducing Broker	BTIG, LLC
Clearing & Custodian	Pershing, LLC
Administrator	Opus Fund Services, LLC
Legal Counsel	Sadis & Goldberg LLP
Auditor	CohnReznick LLP

December 2023 Commentary

Dear partners and friends,

Desert Lion's Fund returned +4.3% for the month of December, bringing its returns to +4.7% for the fourth quarter, and -6.1% for the full year of 2023. Our portfolio return itself was positive, but the exchange rate posed a headwind with the ZAR depreciating -7% against the USD.

As we remarked in a previous letter,

> *In developed markets, stocks often take the stairs up and the elevator down. In the South African stock market, it is the other way around.*

In the past, I have remarked that temperament is a crucial characteristic of a good portfolio manager. It can be lonely at times to remain steadfastly focused on what I deem to be exciting long-term opportunities in the South African small- and mid-cap space, especially as managers in other markets post double-digit positive returns. And yet, as I will share further below in this letter, our portfolio is full of high-quality companies with incredibly cheap valuations. As a value-sensitive investor with decades of experience in the fluctuations of the SA market vs. the world, how can I *not* be excited?

SA Investor Trip – April 2024

If you are interested in a fertile hunting ground where the quality of the companies and the quality of the management are extremely compelling relative to valuations, then we suggest you join us on our upcoming SA investor trip.

From Monday, April 8th to Wednesday, April 10th, our guests will experience the South African business environment, the ingenuity with which management teams address its unique challenges in profitable ways, and the hospitality of Cape Town as part of an intimate group of thoughtful people. We have quality guests from places like Dubai, Hong Kong, Germany, and Switzerland. The trip will be especially valuable and paradigm-shifting to those who have never visited South Africa before.

The last 2 years…

… in the South African equity market have been a relentless grind of valuation multiple compression and exchange rate headwinds that battered marked-to-market performance, a phenomenon particularly conspicuous in the mid- and small-cap space.

Global allocators shifted from being apathetic about SA equities to being actively averse, resulting in a liquidity withdrawal from SA equity and bond markets on a scale not seen in decades.

The selling was accelerated by a confluence of factors, many of which were political-economical "own goals" scored as manifestation of the ineptitude of the state and the governing party. Think of electricity power outages, failing parastatals, and the government's ideologically misplaced geopolitical dealings.

Then, of course, on the allocators' side, there is the very real consideration of career risk. Why would anyone dependent on a regular paycheck risk the ridicule of making the contrarian bet of allocating to SA equities? The trade of the past decade has been to allocate to large cap U.S. stocks. As JM Keynes remarked, "Worldly wisdom teaches us that it is better for reputation to fail conventionally than to succeed unconventionally." Unlikely that managers will lose their jobs allocating to the now-named "Magnificent 7." So global allocators have been withdrawing funds from and actively avoiding SA equities, fueling indiscriminate selling.

On top of these global headwinds, a regulatory change in the SA fund management space contributed to further indiscriminate selling locally. Applicable to asset managers in South Africa, Regulation 28 limits asset managers' allocations of funds to certain asset classes, including equities, property, and foreign assets. Until recently, offshore (non-SA) exposure was limited to 30%. With that limit now increased to 45%, many funds based in South Africa have been selling down their SA equity exposure, predominantly mid- and small-cap equities, in order to increase offshore exposure towards the new maximum.

So what?

As investors we cannot drive forwards by looking in the rearview mirror. We must attempt to determine a logical array of possible future outcomes and assign what we deem to be reasonable probabilities to each.

A balanced assessment of the SA equity opportunity set today suggests that there are sufficient opportunities within the universe to construct an asymmetric portfolio with upside convexity. The last 2 years of performance have been disappointing on an absolute basis. However, this has been driven not as much by business deterioration as it has by multiple compression. Encouragingly, a challenging operating environment elevated and accelerated the natural selection process of survival of the fittest. The winners have been slashing debt, optimizing efficiencies, improving capital allocation – to the point where many companies are now of higher quality than they were pre-COVID. Still, their multiples have never been as low. Again, the phenomenon is most apparent in the most inefficient segment of the market. The small- and mid-cap space has seen an exodus of analyst and buyside coverage and is riddled with skeletons of wound-up funds and scarred retail investors… effectively abandoned, deserted, and inscribed "all hope abandon ye who enter here"…

Yet, in evaluating our current portfolio, we conclude that it is <u>not</u> logical to abandon all hope.

If one were to view our portfolio as one diversified business, constituting the weighted contributions of the underlying portfolio companies, the metrics are as follows:

- Year-on-year earnings growth of +12% (more commentary on this below).
- Return on ending equity of 14%.
- Price earnings multiple of 5x (where earnings essentially approximate after-tax cash flows).
- Therefore, earnings yield of 20%.

Company	Portfolio %	YoY EPS	RoE	PE
Argent Industrial	*	22%	16%	3
Calgro M3	*	77%	14%	2
KAL Group	*	7%	15%	6
Karooooo	*	35%	29%	19
Lewis	*	-8%	10%	5
Master Drilling	*	10%	12%	5
Mustek	*	5%	14%	3
Nu-World	*	-16%	5%	8
Sibanye-Stillwater	*	-48%	12%	5
Stadio	*	20%	11%	21
Zeda	*	31%	31%	3
Weighted Average		**12%**	**14%**	**5**

We are providing the above, warts and all. Perspicacious readers will notice Sibanye Stillwater's negative earnings growth of -48%. Alas, this was a mistake by your fund manager, a painful reminder to him of why a much larger margin of safety is required when it comes to investing in mining companies.

Now, if we were to strip out Sibanye Stillwater – not in an effort to absolve the sins of your fund manager, but to reflect the intrinsic quality of the rest of the portfolio – we are presented with some appealing metrics. An investor in the Fund invests in a "business" with:

- Year-on-year earnings growth of **+21%**.
- Return on ending equity of **14%**.
- Price earnings multiple of **5x** (where earnings essentially approximate after-tax cash flows).
- Therefore, earnings yield of **20%**.

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In Closing

All investing involves risk. The question is, is it highly correlated risk or less correlated risk, and are you being sufficiently compensated for the risk? Our Fund's current portfolio satisfies the criteria: analysis suggests minimal downside risk with meaningful upside convexity should just one or a few of many factors change state from the presently abhorrent to just not-so-bad.

As always, I thank you for entrusting Desert Lion with your hard-earned capital. The majority of my wealth is invested in the Fund right alongside you.

All the best,

Rudi van Niekerk

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