CONSEQUENCE
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Talking Points
What will the next chapter hold for Naspers?

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For Financial Advisors and their Clients

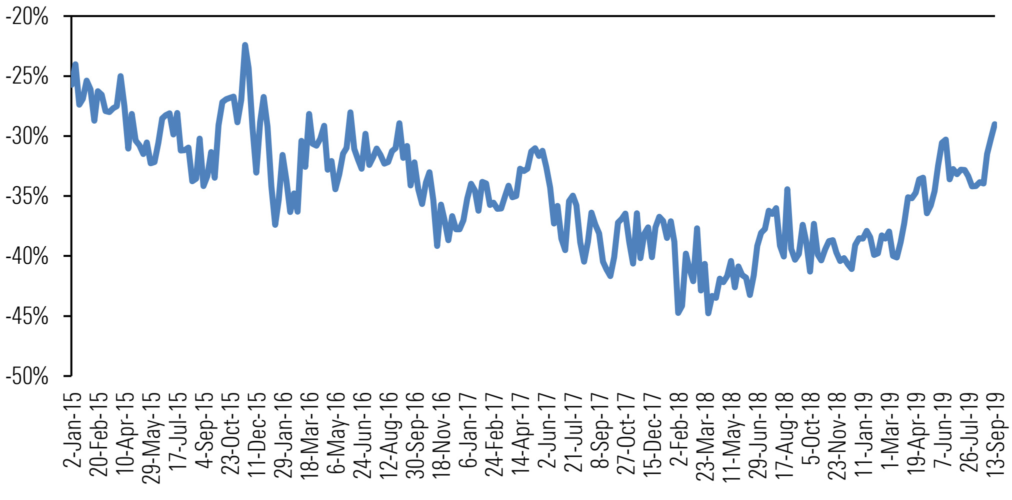
On Wednesday, 11 September 2019, Prosus was listed on the Euronext stock exchange in Amsterdam. Prosus is now Europe's largest consumer internet firm. Cape Town based Naspers will still own about 74% of Prosus, while floating the remaining 26%. Prosus houses Naspers' foreign assets such as Tencent, OLX, mail.ru, Avito, Letgo, iFood, PayU, Swiggy, Udemy, MakeMyTrip, eMag and DeliveryHero.

Gerbrandt Kruger, senior investment analyst at Morningstar Investment Management South Africa, herein shares his insights on what the change means for investors.

Why did Naspers decide to unbundle their offshore assets?

Holding companies, like Naspers, can often trade at a discount to the sum of the underlying companies for various reasons. An example would be holding private companies that are difficult to value. The discount on the Naspers share price - i.e. the sum of its assets was far greater than its market capitalisation - reached such a level that it placed pressure on management to reduce this discount by unbundling the underlying holdings.

The below graph illustrates Naspers' holding company discount to Net Asset Value (NAV) - pre and post Prosus listing announcement:

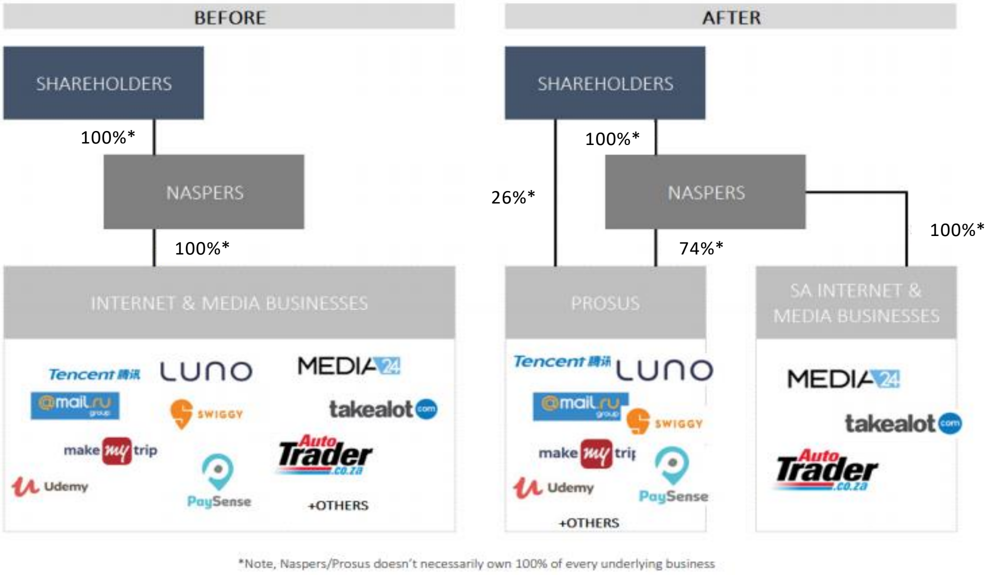


Source: Bloomberg, Investec Asset Management as at 13 September 2019
Note: Naspers announced its intention to list Prosus on 25 March 2019

The first step Naspers took to unlock this value happened earlier this year with the unbundling of Multichoice and its separate listing on the JSE. The latest step by management was to list the offshore assets on the Euronext bourse in Amsterdam via a new company called Prosus. Prosus will be the third-largest company by market cap on the Euronext exchange and the eighth largest by trade volume. By listing outside of South Africa, the investor base of Prosus will be broadened, by having a primary listing in Europe.

What are the underlying companies of Naspers and Prosus after the unbundling?

The local assets (Media24, Takealot and Autotrader) will remain with Naspers and Naspers will own 74% of Prosus. The foreign assets will be housed in Prosus, the likes of Tencent, mail.ru and OLX.



Source: http://finbofs.com/mind-the-gap-how-naspers-is-trying-to-close-its-valuation-discount/

What is the impact of the unbundling on indices?

For some time, Naspers has been the elephant in the room with its large weighting in South African indices dominating returns. Prior to the new listing, Naspers represented roughly 25% of the JSE Shareholder Weighted Index (SWIX) and 18% of the JSE All Share Index (ALSI). With this unbundling, Naspers' size in most market cap weighted indices will reduce on face value. However, the net effect of the change will be neutral for the ALSI and SWIX as the drop-in weight of Naspers will be taken up by Prosus. For example, it is expected that Naspers' weight in the JSE All Share will reduce between 3% and 5% and that Prosus will be included at a weighting of between 3% and 5% (depending on its market cap). For the capped indices, such as the Capped SWIX and S&P SA Top 50, Naspers' weighting will remain around a 10% capped amount, but Prosus will be included. This will lead to an "increased" allocation to Naspers and Naspers-linked companies.

Prosus will now also be part of the AEX All Share Index, due to it being the third biggest company by market cap on the Euronext exchange. Prosus will also be included in other developed market indices. This could potentially lead to flows from passive funds that track these indices. The new company will not be included in the MSCI South Africa Index, that is used by foreign investors as a proxy for SA Equities, as the primary company listing isn't in South Africa. Naspers will, therefore, reduce in weight from 32% to 24%.

What does this mean for investors?

Investors who had a meaningful exposure to Naspers shares will see a drop in the holding of Naspers in their portfolios but will likely see the introduction of Prosus in their portfolios. The net effect is likely to be that investors will be in the same position as they were prior to the listing. This may change over time as fund managers choose to change their positions, but the unbundling will not negatively impact investors.

Prosus or Naspers?

While almost all investors (96%) chose the default option and received Prosus shares, this doesn't mean that there is no investment case for Naspers. Investors now have optionality. Depending on their views and where they see value going forward, they can decide to either invest in the S.A. focused Naspers or the globally focused Prosus. A handful of fund managers made the decision to switch some of their Naspers exposure to Prosus - mainly to get "cleaner" Tencent exposure.

Unfortunately, the change isn't all positive. It is unfortunate that management decided to copy the dual shareholding structure of Naspers for Prosus. In Naspers' case the unlisted A-shares carry 1000 votes per share compared to the 1 vote per share the listed N-shares carry. This will ultimately sway the balance of power to investors that hold the A-shares. This structure could see some of the governance, management accountability and transparency issues that were raised around Naspers be carried over to the new company.

Some fund managers have decided to err on the side of caution by opting to hold both and wait and see what management's plans are for Naspers. Naspers will inevitably become more South African focused over time. With that said, there is still very little value placed on the local assets. The holding company discount could possibly grow larger for Naspers as there is now an additional holding company between Naspers and Tencent. More scrutiny will be placed on Naspers to manage the local core assets and show that these companies can be profitable.

In Conclusion

Concerns remain regarding the Naspers dual share structure and voting rights and this same structure has effectively been replicated in Prosus. For the valuation gap to reduce (for Prosus), the shares need to attract international investors. The double holding structure of Tencent via Naspers could prove to be an additional headwind.

Prosus will be included in the JSE indices, so instead of having one large entity in Naspers we will now have two slightly smaller entities. Which, when combined, could be bigger if the valuation gap decreases. There will be no real reduction of concentration risk on the JSE All Share.

Only time will tell if management will be successful in achieving the goals that they have set out to achieve.

Risk Warnings

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