NORTHSTAR
ASSET MANAGEMENT

Client Letter 28 October 2013

Quarter End: 30th September 2013

I find it difficult to believe that I am writing my fourth Northstar client report and that we are entering the final quarter of 2013. It has been such a busy year and began on such a tragic note, but we regained our footing and Northstar has, fortunately, enjoyed many new highs. This we ascribe to your patronage!

October will always be etched in history as a solemn month for us - our clients, our staff and everyone that constitutes the Northstar family. Yet it also represents a moment in time when a special person handed down a challenge to us all - to maintain the fine DNA which constitutes Northstar Asset Management, to build-out on the solid foundations laid over two decades and to improve the business wherever we deemed necessary. I believe Alexander would be proud of Northstar today!

There is not one element of the original Northstar formula from which we have deviated, including the manner in which we invest, the desire to have direct relationships with our clients and the nature and style of our communication. Northstar's company principles epitomize who we are and what we believe, namely:

- Our clients are the essence of our business
- Integrity and honesty form the bedrock of our value system
- Our greatest assets are our clients, our people, our performance history and our reputation
- We choose to be the best and not the biggest

Having said this, the vulnerability of the business became patently clear in October 2012 and we realized that Northstar needed reinforcing. Over the past year, we have invested into each area of the business and now have a full research team that spend each and every day finding investment opportunities for our clients. We have also added staff in our operations department to solidify our administration. On technology, we are systematically removing vulnerable, historically manual processes and replacing these with automated systems. Each addition has made Northstar a better business - one which is less dependent on a single person and will ensure credible and sustaining long-term investment performance, thereby releasing some of us to remain closely connected to our clients.

I would like to end this letter with a big ''thank you'' to you, our client. Northstar would not be in the position it is today – a stronger business – had it not been for your ongoing faith in us. An asset manager can only function normally with a stable client base that backs it over long periods of time and we are most appreciative that we have had exactly this. We hope that from our efforts over the past year, you feel that we have done justice to the faith you have placed in Northstar.

Yours sincerely

Adrian Clayton
and the Northstar Investment Team

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Our third quarterly report for 2013 is going to focus on two important subjects. The first is the Investment Process at Northstar Asset Management and will explain how we go about selecting which investments to place into our clients' portfolios. The second is why we own Standard Bank in our portfolios.

The Investment Process at Northstar Asset Management:

One of the questions I often ask my friends who are also investment professionals, is how do they know where to begin their research process? This is very important considering the breadth and depth of assets that can be included within an investment portfolio (as an example, we can access financial data for more than 65 000 companies on Bloomberg – which is one of the data suppliers we use at Northstar). Deciding where to begin research is further complicated by market 'noise' which is created by market participants in order to generate business and is also heavily driven by the media.

The most respected global investment managers have demonstrated an ability to build wealth for their clients by adopting a systematic and logical framework to manage money. This is often referred to as an investment process. It is a repeatable, factory-like process that can be easily explained and creates the central thread around which the entire business operates. Critically, it is not dependent on one person and like any good process, can be taught to new entrants. An investment process does not guarantee top returns each year - the market operates randomly over such short time periods and many managers without a process that perform well over short bursts are fooled into believing that their gains are easily repeatable. However, what a robust and logical process does guarantee is consistency of returns over the long-term and the assurance that a manager knows an asset's worth rather than simply injecting overvalued investments into their clients' portfolios.

At Northstar, we have exactly this system working in the background. We feel that we owe it to our clients to have a thorough structure which is followed by all the analysts, week in and week out. What follows is a very brief description of how we manage our equity selections. A good starting point is our end objective.

Our entire year focuses on constructing two ''Buy Lists'', one with 25 offshore companies and another with 25 domestic companies. These are our preferred companies and we know these businesses backwards. It is from these lists that our client portfolios are constructed. Arriving at this list of 50 companies follows a number of structured steps:

1. Reduce the research universe to a manageable number

The potential stock universe, as mentioned above, consists of 65 000 offshore companies and the entire JSE, with particular focus on the top 165 stocks on our market. Our first task is to reduce the offshore stocks to 2000 companies based on their market size (market capitalization), so we select the 2000 largest companies in the world. From our experience, our clients are not interested in owning high risk, marginal companies and we see little merit in expending large amounts of energy on these types of investments.

2. Screen on value, quality and prospective returns

You will notice that all our Northstar marketing material contains three 'catch words' – Time| Value| Quality. This is not simply a marketing ploy - it reflects our investment process and what follows is an explanation of how these three words fit into the bigger scheme of things. We implement a quantitative process where we screen or filter the 2000 offshore companies and 165 local companies using financial ratios that represent QUALITY aspects and VALUE aspects. We also utilize another screening technique in which we rank all these companies on our own, in-house-designed, PROSPECTIVE RETURNS screen. We are thus ranking these many companies on three measures – the quality of the company, how cheap they are (their value) and what expected returns we believe they can generate over the next three years.

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3. The cross over idea list

Having completed the task of ranking all companies on the three measures above, we then create a short list of companies that score across all these attributes – quality, value and prospective returns. This compiled list is significantly smaller and, in fact, consists of just over 100 stocks. It is from this list that we select the companies for an initial 'shallow-dive'. A shallow dive simply implies an initial assessment of the firm. It precedes research which requires studying the business in great depth – what we refer to as a 'deep dive'.

4. Shallow dive decisions

The companies which will undergo a shallow dive have specific characteristics, including:

4.1 They rank highly on our ranking lists. In other words, these companies are those that are QUALITY businesses, offer VALUE (the value of the business exceeds the price at which it is trading at) and future PROSPECTIVE RETURNS are high.

4.2 They exist in industries we like. These are industries with high barriers to entry where companies enjoy high returns/high levels of profitability relative to invested capital.

4.3 They are businesses which we might already know, understand and have undertaken research into in the past.

5. Deep dive decisions

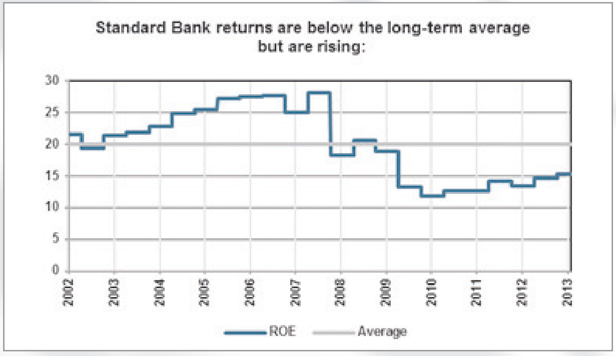
This entire process culminates in a short list of companies into which our analysts at Northstar undertake in-depth research. Each company requires approximately 100 hours of work before we feel that we know it well enough to include it onto our buy list and in turn, into our clients' portfolios.

This intense process demonstrates just how seriously we take our objective of building deep insights into every investment we make on behalf of our clients. At Northstar, we believe in the old adage that successful investing takes homework and not guesswork!

Five reasons why we own Standard Bank:

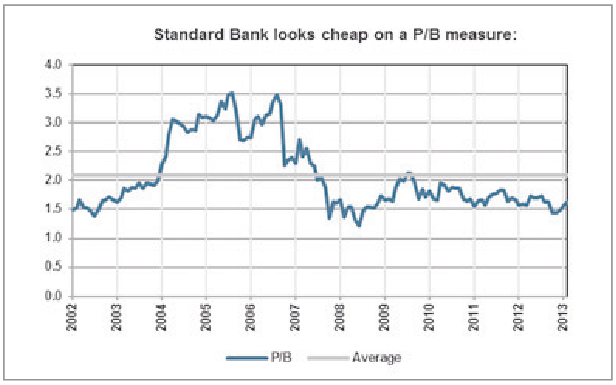
Since joining Northstar In December 2012, Standard Bank is the third company to feature in our Market Report. The first was Sasol, which has gained an incredible 32% (Dec 2012 report) versus the market's 12% rise. The second was Anglos (featured in March 2013) which initially fell then rallied hard and, to date, is level since our report. We believe Anglos is worth substantially more than it presently is trading at.

Standard Bank has been an active addition to our portfolios this past year. What follows is a very brief summary, in the form of five reasons why we own Standard Bank.



1. Financials are cheaper than other parts of the JSE. From our prospective returns screening process, financial stocks are showing better future returns than other parts of the domestic market. Large portions of our market are no longer that cheap and whilst financials have been better value in the past (such as in the crisis in 2008), they are still relatively inexpensive compared to particularly industrial shares on the JSE.

2. Standard Bank has a high cost base which is being attacked by new management. The Standard Bank management team has expressed an intention to reduce expenses and are cutting out unproductive and expensive parts of the business (such as their London office). Consequently, we believe the bank is likely to become leaner in the years ahead and thus provide better returns for shareholders. We feel (and there are technical reasons for this) that the bank's cost to income ratio, which is almost 58%, is too high and pressure will be placed on management to reduce this.



3. Standard Bank is undervalued. Since we initiated our aggressive buying program a few months ago, the stock has climbed by a rather precipitous 21% and is certainly not quite as cheap as when we first started buying. However, on all measures considered, Standard Bank does not reflect the inherent value within the company. Even on simple measures such as P/B (1.7 times) versus Return on Equity (15.4%) and P/E (11.7), Standard Bank offered excellent value.

4. The business has faced headwinds which might turn to tail winds. Standard Bank - as is the case for all banks in South Africa - would not perform well in a rapidly rising and progressive interest rate environment. This is because debtors would default on their loans. However, should interest rates rise marginally, this could be beneficial to the bank. Very simply, the bank has large amounts of capital that produces low returns when interest rates are low, known as the endowment effect. In a slightly higher rate environment, these returns rise and feed through to the profits of the business.

5. Standard Bank has built an extensive African footprint and in various markets has become the go-to operator. Major markets in which it is dominant include Ghana, Angola and Nigeria and whilst this investment has been funded by patient shareholders for a few years now, the merits of the strategy are now paying dividends. The growth in the African business over the past year has translated into a 38% increase in income and a 67% increase in earnings (FY2012 HEPS) and we believe that this could be the start of creating a sizeable franchise.

Adrian Clayton and the Northstar Investment Team