MERGENCE
INVESTMENT MANAGERS

Resilient REIT

Corporate Governance Concerns

For more information

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Index

Introduction

The Resilient group of companies (Resilient, Fortress, Greenbay and NEPI Rockcastle) are a related group of listed property companies that have grown exceptionally over the past decade though acquisition and aggressive share issuance. We believe that the Resilient stable of companies have engaged in multiple efforts to increase their share price and then to issue shares to raise large amounts of capital at a premium to NAV. The share prices of these companies have fallen significantly over the past three months on the back of a leaked comprehensive research report written by 36One Asset Management. Resilient has taken some steps to address some of the concerns raised regarding the company structure and trading in the company's shares. Despite the share prices of these companies trading much closer to their NAVs and the recently announced board actions, we believe there are still a number of corporate governance concerns that need to be addressed. We outline some of these concerns in this report.

- We are concerned that the Siyakha BEE trust may not qualify as a legitimate BEE scheme and that the company may be found to have engaged in fronting and may be liable for fines.

- The company has used a number of accounts that are ostensibly at arm's length to trade large numbers of the company's shares for no discernible reason, raising the concern that these accounts have been used to manipulate the share price or create the illusion of trading volume.

- We illustrate that a close associate of the CEO is linked to a number of these accounts and that this behaviour has been going on for at least 10 years.

- We believe that at least some of the group companies operate in concert and should be treated as associates from the perspective of insider trading regulation.

- A number of group companies and directors were the subject of a police investigation into fraud and market manipulation in 2011. This case has never been resolved.

- Both Resilient and Fortress have relied on one property valuer to value all of their local properties for the past 12 years.

- A number of directors of Resilient have recently moved over R8bn worth of shares out of South Africa to Namibia over the past few months.

BEE Trust

The Siyakha education trusts are the primary BEE shareholders in both Resilient and Fortress REITs. These three trusts own approximately 12% of the shares in Resilient and about 11% of the Fortress B units. The total value of this holding was over R14bn at its peak. With assets of over R14bn and more than a 10% shareholding in (what was until recently) one of corporate South Africa's biggest success stories of the past decade, one would expect Siyakha to have generated significant value for its beneficiaries. Unfortunately, that doesn't seem to be the case.

From what has been disclosed up until December 2017, Siyakha has built three ''learning labs'' in Resilient/Fortress malls, produced a number of newspaper inserts and awarded 28 bursaries since inception. While the trusts have materially increased their shareholding in Resilient and Fortress shares in the past few years, their spending on beneficiaries has reduced, from a disclosed spending of R41.5m in 2015 and R74m in 2016[i] to a disclosed operating budget of R20m for 2018[ii]. This is despite holding shares to the value of R14.5bn as at December 2017 with projected dividends of over R700m and while paying nearly R800m in interest to Resilient and Fortress in 2017. Despite recent share price falls, directors and their associates have generated significant wealth through Resilient and Fortress and yet their largest BEE shareholder is now left technically bankrupt with an estimated negative equity value of over R3bn.

We believe that the legitimacy of the Siyakha Trusts as BEE shareholders in Resilient and Fortress needs to be investigated due to the following:

- We challenge the independence of the trustees due to numerous links to Resilient and Fortress as well as the ability of Resilient to remove any trustees at will.
- The trust has been managed in a financially irresponsible manner with leverage increasing to levels above 400% and the trusts currently in a negative equity position of more than R3bn.
- The BEE verification agency that issued the Resilient and Fortress BEE certificates is under investigation by the BEE commission.
- We believe that the benefit that has accrued to Resilient and Fortress from the Trusts has far outweighed the amounts that the trusts have spent on their beneficiaries.

Independence of directors

The BEE codes of best practice require trustees of a BEE trust to meet the following criteria:
- 50% of the trustees must be black
- 50% of the trustees must be independent
- 85% of the economic benefit of the trust must accrue to black beneficiaries

While Siyakha states that it complies with these requirements we believe this can be challenged.

The Siyakha Education Trust deed includes a clause that allows the founder of the trust (Resilient) to remove any one of the trustees and replace them. As far as we can tell the only restriction on this ability is that the composition of the trustees meet the criteria of the trust deed, including 50% of the trustees must be black, at least one of the trustees must be a black woman and at least 50% of the trustees must be independent.

> 4.5. The Founder shall be entitled to remove any Trustee by giving him written notice to that effect, and to fill any vacancy created by such removal, provided that in removing such Trustee and filling such vacancy the Founder shall ensure that the provisions of clause 4.4 are adhered to. If at any time there are less than 3 (three) Trustees in office, the Founder will, subject to the provisions set out in clause 4.4, immediately appoint any replacement Trustee to succeed a Trustee who ceases to hold office as a Trustee.

Source: Siyakha Education Trust Deed

We believe that this materially impairs the independence of these trustees as Resilient theoretically has the ability to remove any trustee that acts contrary to their wishes.

The following trustees have been in place at the three Siyakha trusts.

Name of trust	Trustees	Date of appointment
The Siyakha Education Trust	Dazray Tarr	23 May 2013
	Jacques Johannes van Wyk	26 November 2012
	Leeone Phoebe Gindan	13 October 2017
The Siyakha 1 Education Trust	Dazray Tarr	13 December 2016
	Jacques Johannes van Wyk	13 December 2016
	Leeone Phoebe Gindan	6 July 2017
The Siyakha 2 Education Trust	Tshiamo Daphne Vilakazi	13 December 2016
	Ndhlabole Shongwe	13 December 2016
	Leeone Phoebe Gindan	13 December 2016

Source: Resilient FAQ

In addition, Tembi Chagonda served on Siyakha Education Trust and Siyakha 1 Education Trust until 1 March 2017.

We illustrate below that many of these trustees have links to Fortress and Resilient and in many cases these links call their independence into question:

- **Jacques Johannes van Wyk**
  Mr van Wyk is an ex-CFO of Resilient. While the board claims that Mr van Wyk is independent of Resilient, shareholder registers show that Mr van Wyk holds a significant number of shares in Resilient and NEPI Rockcastle. Our analysis of shareholders registers shows that multiple accounts under the name of Mr Jacquess Johannes van Wyk held shares that had an aggregate value of over R450m in these two counters as at December 2017, with over R300m of that value in Resilient shares. It is our view that any individual with such a significant shareholding in a company cannot be considered independent of that company. We believe that Mr van Wyk has a material conflict of interest between his duty to the Siyakha trusts and his material personal exposure to the Resilient share price. Resilient has disclosed that Mr Van Wyk's appointment has been to ensure that there is sufficient financial expertise on the board of trustees of the Siyakha trusts on which he serves. We therefore view the financial decisions taken by the trusts on which he serves as being representative of a large degree of influence from Mr Van Wyk.

- **Dazray Tarr**
  Ms Tarr is an employee of Resilient and serves as the office manager of Resilient REIT. We believe that Ms Tarr cannot be considered independent given her employment by Resilient.

- **Leonie Gindan**
  Ms Gindan was the company secretary for Lodestone REIT until at least December 2016. We have not been able to establish if she is still employed by Loadstone, but both her LinkedIn and Facebook profiles suggest that this is the case. According to SENS announcements Ms Gindan was a shareholder in Lodestone[iii] and elected to convert those shares to Resilient shares at the date of the acquisition[iv].

The offer from Fortress to acquire Lodestone closed on 9 December 2016[v] and Ms Gindan was appointed as a director of the The Siyakha 2 Education Trust on the 13 December 2016. In our view Ms Gindan cannot be considered independent.

- **Thembi Chagonda**
  Ms Chagonda has been a director of Resilient since 2008. She resigned as a trustee of the Siyakha trusts on the 1 March 2017 after she was appointed Chairperson of Resilient. While Ms Chagonda resigned post her appointment as chairperson of Resilient she served as a trustee while a non-executive director of Resilient which we still believe challenges her independence during that time.

- **Tchiamo Vilakazi**
  Ms Vilakazi is a shareholder in Emerging African Property Holdings (EAPH) and has served as a non-executive director of Fortress since December 2015[vi]. EAPH was a shareholder in Eagle's Eye Investments, a BEE investor in Resilient over the ten-year period up until June 2016. According to share registers EAPH maintained a shareholding in Resilient up until August 2017.

- **Ndhlabole Shongwe**
  Mr Shongwe is a former non-executive director of Lodestone REIT.

Furthermore, it is disclosed that Ms Chagonda resigned from the boards of Siyakha Education Trust and Siyakha 1 Education Trust on the 1 March 2017 and yet her replacements where only appointed months later in October 2017 for the Siyakha Education Trust and July 2017 for the Siyakha 1 Education Trust. This means that the trust was in breach of the requirements of its own trust dead over the intervening period, which states that the trust must have at least three trustees at all times. It is important to note that, according to disclosure in the Resilient FAQ, the Siyakha Education trust traded a significant number of FFB shares during this period[vii].

It is our view that both Siyakha Education Trust and Siyakha 1 Education Trust have not met the requirement of 50% independent directors since their founding and that this view is further supported by the financial decisions made by the trustees and the resultant financial situation these trusts have been left in.

Financial situation

It is our view that the Siyakha trusts have been created through an unsustainable financing arrangement with Resilient and Fortress that requires the share prices of these holdings to rise for the trusts to remain solvent. The trusts raised about R3.5bn of external funding from external funders including Standard Bank[viii] with the remainder of the debt funding coming from Resilient and Fortress. These loans are then used to buy shares in Resilient and Fortress.

As described so far, this arrangement is not unusual. Normally a BEE investor in this situation would use dividends earned on the shares they hold to partly service interest on their debt and over time the dividend and capital growth on the shares would allow the BEE shareholder to repay the debt and realise a net capital gain. Unfortunately, the Siyakha trusts paid interest at a rate of up to prime plus 2% to Resilient and Fortress on these loans and did not accrue or ''roll up'' any of their interest payments, but rather paid interest in full immediately.

The problem was that while they were servicing debt at an interest rate of prime plus 2% (about 12%) they were earning dividends at a yield of about 5%-6% on the shares they purchased. The result was that the trusts were immediately in a negative cashflow position and needed the shares they owned to rise in price to remain solvent. On the other side of the transaction this deal has been cashflow accretive to Resilient and Fortress. They issue shares at a yield of 5%-6% and receive interest back at a rate of prime plus 2%. This situation has been supportive of both company's distribution growth.

Secondly, the trusts have consistently increased their borrowings to buy more and more Resilient and Fortress shares at higher and higher prices. The result has been that the gearing of the trusts peaked at a debt to equity ratio of 372% in 2017. We question why a trust with a 2018 operating budget of R20m[ix] saw any need to borrow a total of R10bn to buy R14bn worth of shares and to continue to buy these shares even as the cash flow situation of the trust became clearly untenable.

The results of this extreme level of gearing is that while Resilient could confidently state that the Siyakha trusts had a NAV of R4.9bn as at 31 December 2017, as the share prices of Resilient and Fortress fell in the first two months of 2018 this value was quickly wiped out and we estimate the trusts are now in a negative equity position of more than R3bn. Furthermore, the trusts have been forced to go from buyers to sellers of these shares to repay bank debt, realising a loss on shares that they purchased only months ago at higher prices.

In its most recent set of results Resilient has indicated that the board has requested the Siyakha trusts accelerate repayment of their loans from Resilient. This is a strange request for any lender to make to an independent borrower and more so to an empowerment trust. We believe that this again illustrates the lack of independence between Resilient and the Siyakha trusts and the lack of commitment to genuine empowerment.

Given that the Siyakha trusts have now become sellers of shares the trust has effectively become an off-balance sheet funding vehicle for Resilient and Fortress enabling them to support their cashflow.

Resilient and Fortress issue share to Siyakha. Siyakha uses these shares to raise scrip backed funding from commercial banks and uses some that cash to pay interest back to Resilient and Fortress. The trust funds their interest payments for a period of time but eventually sells the shares to repay interest and loans to Resilient and Fortress. In both of these cases Resilient and Fortress have converted issued shares into interest income.

Spending on beneficiaries

In 2015 and 2016 Resilient disclosed the total spending of the Siyakha trust as R41m and R74m respectively. This was spent on renovating facilities at under privileged schools, building three learning labs in Resilient and Fortress Malls and producing some free educational content distributed in newspapers. In the 2017 annual report Resilient does not disclose the spending by the trusts on their beneficiaries but states that the focus of the trusts has changed to providing bursaries to tertiary students and that the trusts awarded 28 bursaries in 2017 and had approved a further 108 for 2018. In a recent SENS announcement, it was disclosed that the trusts operating budget for 2018 was R20m.

We find it strange that a trust that has so aggressively increased its shareholding in Resilient and Fortress since 2015, is now budgeted to spend less on its beneficiaries in 2018 than it did in 2015. This is even more stark when we compare the interest bill of the trust compared to the spending on beneficiaries. We estimate that the Siyakha trusts paid nearly R800m in interest to Resilient and Fortress in 2017.

	2018/Current	2017	2016	2015	2014
Total value of shares held	6,488	12,075	10,553	4,840	1,385
Total debt	10,008	9,515	7,213	2,840	747
Dividends received	691	540	316	126	73
Interest paid to RES, Fortress	813	793	375	141	72
Interest on bank funding	353	263	263	88	-
Siyakha Spending	20	Not disclosed	74	42	29
NAV	-3,520.43	2,560	3,340	2,000	Not Disclosed
Debt to Equity		3.72	2.16	1.42	

Source: Company Financial Statements, Mergence calculations

- *All figures in Rm*
- *Current Values based on shares prices as at 12 March 2018*
- *Dividends received and interest paid are estimated based on shares held at the beginning and end of reporting periods and estimated cost of funding for external funding*
- *Current NAV is an estimate based on assumptions regarding Siyakha share trades since last disclosure and is subject to estimation error*

Resilient's BEE verification agency is under investigation

According to a media release on 7 August 2017, the B-BBEE commission is investigating Premier Verification, the agency responsible for both Resilient and Fortress's BEE certification[x]. The scope of the investigation is to:

"*Determine whether the black ownership structure of the verification agency complies with the black ownership requirements and whether in its conduct of verification it follows the procedures required of a verification agency and the verification professionals in line with the B-BBEE Act.*"

Trade in group company shares

Following recent announcements by Resilient Income Fund as well as the emergence of two reports on the company we believe that there are a number of questions that have not been sufficiently answered by the company's responses. The allegations raised by the 36One report are similar to those raised previously by investigative journalist Martin Welz at Noseweek and thus require further scrutiny.

As raised by both Navigare Securities and the 36One report leaked on the 9th of February, four companies K2012040925, K2012040668, K2012040151 and K2012040929 have traded significant numbers of shares of the Resilient group companies over the past year. These companies all have a common director Hendrik

Johannes Oberholzer listed as their sole director at CIPC. In a SENS announcement on the 5th February 2018[xi] Resilient stated that:

"The board and management of Resilient, and Resilient itself, have no interest in or arrangement of any sort with the private companies or director in question."

In the SENS announcement dated 12th February 2018[xii] the company stated:

"Mr HJ Oberholzer is known to the Company as a manager of substantial private investments, representing principals who have long invested in Resilient and the companies it is invested in. No member of the board or management of Resilient has any interest or involvement in these investing activities."

CIPC records show that Mr Oberholzer is also a director of a company called Comess. This company has listed as its auditors Du Plessis and Du Plessis, who are also listed as the auditors of Holyrood Investments, related to Mr Desmond de Beer.

On further investigation we have found that Comess also lists Mr Roque Anthony Hafner as a previous director from 1998/04/23 to 2012/10/17.

Company Summary Click to Collapse

Enterprise name	COMESS
Status	IN BUSINESS
Registration number	1997/019830/07
Registration date	1997/11/20

Additional searches available

Deeds Office Company	Search	TransUnion Business Profile	Search
WinDeed Spider	Search	Judgment Enquiry	Search
VAT Number	Search	Bank Account Verification	Search
WinDeed Alerts	Request		

Director and Other Summary Click to Collapse

Active

Name	ID/Reg Number	Type	Status
OBERHOLZER, HENDRIK JOHANNES	6502095044086	Director	Active
Other possible matches for director			*(Select all possible matches)*
VAN NIEKERK, GERHARDUS DIRK	6305285135007	Director	Active
Other possible matches for director			*(Select all possible matches)*

Inactive

Name	ID/Reg Number	Type	Status
HAFNER, ROQUE ANTHONY	6004275096085	Director	Resigned
Other possible matches for director			*(Select all possible matches)*

Search Selected Directors

Source: Windeed

Furthermore, Mr Hafner is also listed as a previous director on Eco Aire (Pty) Ltd which Mr Oberholzer and Mr Van Niekerk are current shareholders and Mr Hafner and Mr Oberholzer are both listed as directors of a company named Unit 17 Crestleigh. In fact, in the case of Eco Aire, Mr Hafner and Mr Oberholzer are listed with the same residential address.

We find this concerning for a number of reasons:

Mr Hafner has had dealings with Mr Desmond de Beer over a number of years. These include Mr Hafner and Mr De Beer both serving as directors of New Heights 471, which sold properties to Fortress Income Fund in October 2009. Mr Hafner also served as a director of Amber Peek Investments which was extended a loan by Resilient as disclosed in the Resilient 2008 financial statements and according to Noseweek, actively traded in the shares of Resilient Capital Property Fund and Pangbourne Properties[xiii].

Furthermore, according to the judgement in the case ''Durr v Absa Bank Ltd and Another''[xiv] as well as an article written by former professor of auditing at the University of Pretoria, Deon Basson, Mr Hafner previously served as the Financial Director of Supreme Investment Holdings[xv]. Supreme allegedly operated for six years selling debentures to unsuspecting investors while the company was in fact insolvent. According to Noseweek, Mr Hafner was arrested for fraud in 1993.

		GROUP		COMPANY	
		2008 R'000	2007 R'000	2008 R'000	2007 R'000
8	LOANS				
	Unit purchase trust loans (refer to note 22)	169 908	140 141	169 243	139 741
	Other loans	51 885	48 433		
	Loan to Amber Peek Investments (Proprietary) Limited	86 311	–		
	Loan to Gillyfrost 56 (Proprietary) Limited	4 696	–		
		312 800	188 574	169 243	139 741

The unit purchase trust loans and other loans bear interest at the weighted average cost of funding of the group, being 9,49% (2007: 11,29%) at year-end. The loans are secured by 13 395 800 (2007: 12 274 000) linked units in Resilient with a fair value of R316,8 million (2007: R331,4 million). The value of security held for each individual loan exceeds the amount of the related loan.

The loan to Amber Peek Investments (Proprietary) Limited bears interest at prime minus 1%, is unsecured and is repayable on 30 June 2019.

The loan to Gillyfrost 56 (Proprietary) Limited bears interest at prime, is secured by investment property and is repayable on completion of the development known as Burgersfort Mall which is not expected to be completed in 2009.

Resilient 2008 Annual Report

"Amber Peek, it appears from an analysis of net monthly share trades published by I-Net Bridge, used the money it borrowed from Resilient to trade – furiously – in Resilient's own shares and those of three other JSE-listed companies in the Resilient group: Capital Property Fund, Pangbourne Properties and the since- delisted Monyetla.

Between June 2008, when it traded its first R112m-worth of Resilient units, and February 2010, when it sold the last R68m-worth of Resilient units, Amber Peek traded these shares back and forth, generating a turnover in Resilient shares of over R530m.

In the same period and in similar fashion it traded Capital shares worth over R213m, Pangbourne shares worth R435m and Monyetla shares worth R13m.

Based only on month-end balances (there might have been many more trades within a month), Amber Peek succeeded in moving or "churning" a gross trade of at least R1.2bn-worth of Resilient group shares through the market, using just the R86.3m it had borrowed from Resilient for that purpose. (No evidence was found of it having traded in any shares other than those of companies in the Resilient group.) For Resilient's 2008 financial year, Amber Peek's trades accounted for a substantial 14.1% of total volume traded – all of it in the second half of the year. In the following financial year the trades accounted for nearly 12% of total volume of Resilient shares traded on the JSE."

Source: Noseweek Issue #136, 1st February 2011. https://www.noseweek.co.za/article/2422/Roque-trader

What is also concerning is that from what we can see from the Resilient Annual Reports from 2008 to 2010, Amber Peek received a loan from Resilient during 2008. In the 2010 Annual report, Amber Peek is referred to as a BEE vehicle for the first time and it is disclosed that

"Effective 22 April 2010, Sydney Malabie and JJ Njeke obtained a beneficial, indirect holding in Resilient as a result of their participation in a BEE ownership scheme undertaken through Amber Peek Investments (Pty) Ltd."

If Amber Peek only achieved BEE status in 2010 what was the motivation for Resilient financing the company for two years prior to this event?

Secondly, an analysis of the 4 companies K2012040925, K2012040668, K2012040151 and K2012040929 shows that these companies have conducted significant trade in the shares of Resilient, Fortress, Green bay and NEPI Rockcastle over the past 5 months.

Our analysis using end of month holdings and assuming trades at the average of the opening and closing share price over the period, shows that these four entities executed about R2.2bn of trades in these four companies over the period 25 August 2017 to 26 January 2018. Given that the total asset value of these entities was R1.2bn as at 26 January 2018 this is a very high level of turn over. We also note that these trades show no consistent pattern with some months showing trades in opposite directions for the same stock in different accounts. The pattern of these trades suggests strongly that these accounts are not long-term investors in the Resilient group companies but rather active traders and speculators.

Estimated Rand value of change in holdings for K2012040925, K2012040668, K2012040151 and K2012040929

FFB	2018/01/26	2018/01/29	2017/11/24	2017/10/27	2017/09/29
K2012040925	-	23 771 345	-	-	-
K2012040668	-	-61 625 032	-20 910 525	-40 847 042	117 993 429
K2012040151	-	-5 427 000	-6 165 750	-	-7 767 000
K2012040929	-	-	-	-	-
GRP	**2018/01/26**	**2018/01/29**	**2017/11/24**	**2017/10/27**	**2017/09/29**
K2012040925	147 047 080	77 933 678	-1 267 500	-66 279 132	-27 671 091
K2012040668	76 400 000	-31 077 345	-760 500	-2 187 000	-1 122 500
K2012040151	98 581 644	-6 659 570	-34 476 000	-	-
K2012040929	-	2 871 167	-	-	-
RES	**2018/01/26**	**2018/01/29**	**2017/11/24**	**2017/10/27**	**2017/09/29**
K2012040925	24 415 000	16 120 685	-	-	-
K2012040668	71 662 420	-	-	-	-
K2012040151	-	-2 592 000	-6 176 060	-	92 186 105
K2012040929	-	-	-	-33 951 250	123 708 886
NRP	**2018/01/26**	**2018/01/29**	**2017/11/24**	**2017/10/27**	**2017/09/29**
K2012040925	-	-66 884 368	-	68 812 347	-195 603 711
K2012040668	4 153 125	-13 828 875	-2 017 500	68 812 347	-167 518 299
K2012040151	846 905	-48 212 990	-	67 727 643	-228 674 710
K2012040929	-4 153 125	-	-	64 308 300	-42 771 185

Source: Strate, Mergence calculations

We also note that these accounts participated in the May 2017 book build of Greenbay Properties shares. As has already been raised this is concerning that these accounts reportedly sold a significant number of Greenbay shares before this book build only to purchase these shares back in the book build. Our experience of the equity raising process in South African is that management teams have a strong preference for long term holders of company shares and are hesitant to allocate to hedge funds or investors seen as fast money who may immediately sell the shares. It therefore seems strange to us that Greenbay management allocated such a large number of shares to these accounts in the May book build process given their active trading of group shares. In addition, Mr Oberholzer is not registered with the FSB as a licensed financial services provider.

In addition, Mr Hafner is the sole director of a company RCG Trade and Finance that is a significant shareholder of Resilient and related company shares to a value of over R900m at its peak. In fact, when Fortress first listed, the company purchased a property from a company New Heights 471. Mr Hafner was a director of New Heights at the time of this transaction and Mr Desmond De Beer had resigned as a director of New Heights a number of months before. As part of the payment for this property it is claimed that 9m Fortress A and B units were transferred to RCG Trade and Finance. If Mr Hafner is indeed the beneficial owner of this company then he is still highly invested in the group companies and has a strong incentive to ensure that their share prices remain high.

It seems possible to us that Mr Roque Hafner, who seems to be closely associated with Mr Des De Beer, has in the past and continues to, engage in significant trading of shares in the Resilient stable. There are accusations that he conducted this behaviour under the entity Amber Peek during the period 2008 to 2010 using funding from Resilient. Mr Hafner seems to have close ties to Mr HJ Oberholzer who controls entities accused of similar behaviour over the past year. Mr Hafner has been a director of two entities related to Mr HJ Oberholzer and Mr GD Van Niekerk; Comess as well as Eco Aire (Pty) Ltd. In addition, Mr Hafner is the sole director of RCG Trade and Finance, a business which holds close to R1bn of shares in the group companies and shares other links to other material shareholders of Resilient.

We have focussed solely on the trading by the Oberholzer related companies as we believe that the link to Mr Hafner shows a pattern of behaviour that has persisted over years. The report by 36One includes details of various other entities that have also conducted significant trade in Resilient group shares.

We believe that the Resilient group of companies need to address not only the allegations in the most recent reports but also the allegations raised by Noseweek in the past as well as the trading activity in group shares by the companies mentioned above.

The board of Resilient has announced an independent investigation into these allegations, but the scope of this investigation only covers share trading since July 2017. We believe that the scope of the investigation needs to cover all of the allegations levelled against this group of companies and their directors over the past decade. When examined in isolation any one of these instances may be explained away, but when we consider all of the allegations against the group since 2008 a clear pattern of behaviour emerges.

Independence of Resilient and Fortress

While Resilient and Fortress claim to operate independently and have two separate boards that do not share members we believe that the behaviour of the companies illustrate that they operate in concert.

- The company's remuneration policies are almost identical
- The companies have exactly the same BEE structure in place
- Corporate structure and corporate reporting are almost identical
- The companies very often release related SENS announcements within hours of each other

- There is a cross shareholding structure where both companies hold shares in each other
- The company's head offices are located in the same building

This raises significant concerns for minority shareholders as both companies have purchased shares in each other during closed periods. For example, on the 11 of January 2018 both companies released a trading statement within two hours of each other. RES share price rose over 20% and FFB 21% in the hour post the first of these announcements. If these announcements were coordinated their release must have amounted to market sensitive information and these companies should have been restricted from trading in each other's shares over this period.

Previous Police investigation

In 2011 a member of the East Rand Special investigation unit opened an investigation into Resilient and Fortress as well as a number of directors of these companies. As part of this investigation a magistrate granted the investigating officer a subpoena for records from a number of banks and stock brokers. These directors along with a number of banks filed a court application to challenge this subpoena. They were unsuccessful and the judge ruled that the investigation should take place. To the best of our knowledge no further progress has been made on this investigation.[xvi] [xvii]

Property valuations

Much of the debate around the Resilient group of companies has revolved around the high premium to NAV that the companies have traded at in the past. This NAV is generally considered a trustworthy number as it represents the value of actual physical property. One concerning aspect of the Resilient and Fortress NAV is that these companies have relied on the same property valuer, Quadrant Properties, for at least 12 years to value all of the properties that they own. In fact, one company, represented by a single valuer, values over 340 separate properties distributed across the country for the Resilient and Fortress group. A search of the South African Council for the Property Valuers Profession website reveals a total of four registered valuers, one of them a candidate valuer, under Quadrant Properties.[xviii]

Directors share trades

The recently published Resilient FAQ states that three directors restructured their holdings in December 2017 as detailed below.

Associates of senior executives of Resilient restructured their holdings of shares without any change in underlying beneficial interests, as summarised below.

Resilient executive director	Previous associate	Current associate
Andries de Lange	Nano Trust	Dyer Investments (Pty) Ltd (owned by Dyer Trust)
Des de Beer	Hollyrood Investments (Pty) Ltd (owned by Suni Trust)	Delsa Investments (Pty) Ltd (owned by Grove Trust)
Nick Hanekom	Eaglelet Investments (Pty) Ltd (owned by Eaglelet Trust)	Nubie Investments (Pty) Ltd (owned by Zinnia Trust)

The following shares were affected by the restructuring:

RES	28 887 383
NRP	10 756 493
FFB	23 413 045
GRP	236 974 474

What is strange is that in each case the shares have been transferred from South African domiciled companies to Namibian domiciled companies and we question what the rationale for such a move would be. Furthermore, the aggregate value of these transactions is material. Based on closing share prices at the end of December 2017 the shares transferred had a total value of R8.2bn.

We have not been able to find any record of the target companies in South Africa and as per Strate shareholding data each of the target accounts is listed with a country code NA for Namibia.

Company	Country Code
DELSA INVESTMENTS (PTY)LTD	NA
DELSA INVESTMENTS (PTY) LTD	NA
BN1 - *DYER INVESTMENTS (PTY) LTD	NA
DYER INVESTMENTS	NA
NUBIE INVESTMENTS PTY LTD (NO.2)	NA
DYER INVESTMENTS NO.2 (PLEDGE)	NA
NUBIE INVESTMENT PTY LTD	NA
DELSA INVESTMENTS PTY LTD (NO.2)	NA

Company	Country Code
HOLLYROOD INV (PTY) LTD #2 (BEAR SA	ZA
HOLLYROOD INV (PTY) LTD ACC NO 5	ZA
HOLLYROOD INVESTMENTS (PTY) LTD (CE	ZA
HOLLYROOD INVESTMENTS (PTY) LTD ACC	ZA
HOLLYROOD INVESTMENTS (PTY) LTD(NO.	ZA
EAGLELET INVESTMENTS (PTY) LTD	ZA
EAGLELET INVESTMENTS (PTY) LTD - NO	ZA
EAGLELET INVESTMENTS (PTY) LTD (PLE	ZA
EAGLELET INVESTMENTS (PTY) LTD 2	ZA
THE NANO TRUST (PLEDGE)	ZA
THE NANO TRUST ACC 2	ZA
THE NANO TRUST(A/C NO.4)	ZA

Conclusion

We have highlighted a number of corporate governance concerns relating to Resilient and Fortress. We believe there is strong evidence to suggest that the management of Resilient and Fortress have engaged in numerous practices in the attempt to keep their share prices as high as possible and to issue shares at these high prices. It seems to us that the Siyakha trusts have fallen victim to these practices and have been used by management to the benefit of Resilient and Fortress rather than their beneficiaries.

We are of the view that the Siyakha trusts and the BEE status of both Resilient and Fortress need to be investigated.

In our opinion, the investigations into the trading of shares in these companies needs to span the full history of their listings and to take into account the relationships of the individuals involved.

We believe that the scope of the independent investigation at Resilient needs to cover all accusations that have been levelled at the company over the past decade, including the 2011 police investigation.

Disclosure

Mergence Investment Managers holds positions in some of the securities mentioned in this report on behalf of some of our clients. Some of these positions have derivative hedges in place against these positions. Mergence currently has a short position in both RES and FFB in a long short hedge fund. This fund represents less than 0.2% of the total assets managed by Mergence.

This work has been prepared independently by Mergence Investment Managers research team.

We have communicated a number of these concerns to the board of Resilient and have requested comment from the board. We have also requested further information on a number of the issues raised. We have not received any response from the board as at the date of publication of this note. We have also communicated with the board of Fortress who have acknowledged receipt of our concerns and have committed to respond.

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Past performance is not necessarily a guide to future investment performance. Fund performance figures are gross of management fees, net of all applicable withholding & gross of SA capital gains taxes.

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