House View Portfolios Manager Commentary

March 2017

Allan Gray Equity Fund

ASISA Classification

South African - Equity - General

Firm

Allan Gray was founded in 1973 by Allan Gray, initially as a private asset management firm. Allan Gray (Pty) Ltd is the main holding company, with the Life and Unit Trust businesses incorporated in 2000, which laid the foundation for their retail footprint. As at December 2016 the firm had over R495 billion in assets under management with over a 1000 permanently employed staff.

Allan Gray's ownership was previously divided between the Allan Gray family and the executive directors of the company. However, early 2007 saw the launch of E^2, a broad-based black economic empowerment trust. The vehicle is controlled by trustees who are largely independent and it provides financing predominantly to black entrepreneurs. In 2009 Allan Gray finalized an employee share scheme which reserves 14% of shares for current and future staff and of which 10% is earmarked for black staff.

Allan Gray is currently a level 3 contributor to B-BBEE.

Philosophy and process

Allan Gray has maintained their philosophy as valuation-oriented bottom-up investors. The firm buys shares when they are priced below the company's intrinsic value and sells them once the market has adjusted the price to fair value. This reflects an inherent belief that the market is not always efficient or rational, resulting in disparities between the market price and the intrinsic business value of an investment at any given time. Allan Gray's assessment of mispriced opportunities means that they are typically attracted to investments which periodically fall out of favor, giving rise to a somewhat contrarian view.
The research and decision-making processes are built on fundamental proprietary research. The research process is the responsibility of the team of analysts. The portfolio managers keep their ears to the ground by retaining their analyst responsibilities.

Allan Gray, for the South African portfolios, monitors around more than 160 companies which make up their investible universe. Data on all companies is updated in the quantitative model, which is subsequently used to reduce the universe to the target purchase universe of around a 100 shares, based on profitability and marketability, company visits and the international themes which Orbis has identified. This is the first step to identifying superior fundamental value. Portfolio managers and analysts are also free to flag research opportunities outside of the results of the quantitative models, as the firm prides itself on its in-house research capabilities.

The fundamental research is aimed at identifying good quality companies that are trading below their intrinsic value. Detailed share analyses focus on the bottom- up company fundamentals, which include assessments of the company's free-cash flow throughout the economic cycle, the potential for earnings growth, and the strength of balance sheets. Analyses leverage off the up-to-date proprietary database, with information typically extending back over 40 years. The quantitative models use this information to estimate a total rate of return over the next four years viewed in the context of industry fundamentals, any competitive advantages and the track record of a firm's management (particularly when it comes to effective generation of returns on capital for shareholders). The team interacts with management on a regular basis, via calls and visits. The extent to which a share is found to be priced below the intrinsic value, is called the margin of safety. The greater the margin of safety is, the more attractive the share. The intrinsic value is determined predominately through using discounted future cash flows, and the investment horizon is typically four years. Good quality companies are those that can sustain a high level of earnings and dividend growth.

A Policy Group meets twice a month and is made up of all the equity specialists. The portfolio managers are the senior members of the Share Policy Group with Andrew Lapping leading as CIO. The analysts' reports will be presented and after a debate the members of the group will all vote on the share. These votes are ranked by seniority. If a share is voted as a buy, then it will be added to the buy list. It is also given a risk rating. This rating is based on liquidity, profitability and financial risk.

Each of the portfolio managers is allocated a segment of the client portfolios to manage. In the classic equity products, the benchmark is not important to the process and the portfolio is built from scratch. Each portfolio manager has the discretion to hold whichever shares they want from the buy list, but are under no obligation to do so. Orbis is also allocated a portion of the client portfolio to manage. The size of the portions allocated to the portfolio managers is based on seniority, experience and performance track record. The firm therefore effectively employs a form of internal split funding': As portfolio managers manage a portion of a notional pool of funds, and typically not a particular portfolio, clients receive a spread of investment ideas from all the specialist PMs. The process also ameliorates the need for specific back-up persons for key investment personnel. The mechanism, in allocating a greater share to those managers with better track record, can also be seen to foster a spirit of collegial competition. The allocation of trades by the dealing desk is on a first-come, first-serve basis, which also spurs PMS to be clear-sighted and agile in identifying opportunities.

Team

The current team of portfolio managers has been together at Allan Gray for several years now, having started there at approximately the same time. Andrew Lapping took over from Ian Liddle as CIO in 2016. Ian in turn, had been CIO from the time that Stephen Mildenhall departed in 2008 for the UK, having worked alongside one another since 2001. At the time of taking over, Ian Liddle in his capacity as CIO, had already spent considerable time, particularly over the last few years, mentoring the team and ensuring smooth transfers of skills. The Allan Gray team manages assets with a multi councilor approach, which mitigates the key man risk often associated with single or star portfolio managers, while creating additional and intentional diversification within the portfolio. Due to the unchanged philosophy and multi councilor approach, the firm has been able to successfully navigate a number of generational changes.

Product commentary

The South African long-only equity portfolio aims to deliver returns which are superior to the FSE/JSE All Share index, but with a lower risk of capital loss. The portfolio is managed by the same broader team and along the same bottom-up research-driven investment processes as the firm's overall strategy. Lower risk stocks are therefore typically assigned higher ratings on a scale between 1 and 5 stars, which determine the size in the portfolio. The maximum weight of a single holding has been determined as 15%. The mandate for this SA equity product was adjusted in March 2015 to allow for an allocation of 25% to offshore stocks, although the fund presently limits itself to SA-only. The fund, in its new guise, has managed to outperform the benchmark by 3.1% annualized from March 2015 to December 2016

Over the last quarter of 2016, the firm seized on the value opportunities presented by Brexit. It consequently up-weighted its exposure to under-pressure UK-linked stocks such as Old Mutual and Investec, both of which are diversified financial firms which are regarded favorably for their long-term earnings prospects. The firm added to its position in Naspers over the last quarter of 2016, as well as to its exposure to healthcare. Within healthcare, the firm has favored Life Health over beleaguered Mediclinic.

Fees and costs

The minimum investment amount per investor account is R 20 000.

The Total Expense Ratio (TER), a measure of the actual expenses incurred by the Fund over a 3-year period (annualized) includes the annual management fee. It comes to 2.25% for the portfolio, broken up as follows: Fee for benchmark performance (1%) + Performance fee (0.9%) + Other costs (excluding transaction costs, 0.07%) + VAT (0.28%). The Total Investment Charge (TIC) is 2.33% and consists of the TER and the Transaction Cost of 0.08%

Coronation Equity Fund Commentary

ASISA Classification

South African - Equity - General

Firm

Coronation Fund Managers, since its founding in July 1993, have grown to be one of the largest asset management companies in South Africa. The firm is an independent, owner-managed business, which was listed on the JSE in 2003. Coronation Asset Management is a wholly owned subsidiary of Coronation Investment Management SA, itself a wholly owned subsidiary of Coronation Fund Managers. Four other operating entities were established to provide services to a broader client base. These include the Coronation Management Company (RF) (Pty) Ltd, Coronation Life Assurance Company Limited and Coronation Investment Services (Pty) Ltd, as well as the international fund-of-fund business, based in London and Dublin.

The firm’s client base is predominantly institutional (more than 60%) and diversified across asset classes. Pure equity and balanced mandates enjoy considerable focus, being a combined 75% of the AUM. At the end of 2016, the firm had more that R 575 billion under its management.

Coronation is a level 3 contributor to BEE, with black staff holding 10% of shares directly via the Imvula Trust.

Philosophy and process

Coronation is a long-term, valuation driven active manager, with a focus on bottom-up stock picking. The firm considers itself to be style agnostic and adopts a 'clean slate approach' to portfolio construction. The most compelling risk-adjusted stocks based on detailed bottom-up research and fair value assessments of company fundamentals, will make it into a portfolio. Macroeconomic factors are an important input into the research process, as they allow the team to identify mispriced opportunities and gauge future prospects.
In-house fundamental research forms the cornerstone of the investment process and portfolio managers as well as analysts have research responsibilities.

During the research process, the firm attempts to gain a full understanding of the true value of a franchise. Proprietary in-house research is complemented by broker research, tailored surveys and extensive interaction with global and local competitors, customers, suppliers and regulators. Analysts' research responsibilities typically span multiple industry sectors, which allows them to assess relative opportunities. From the top 250 shares of the JSE by market cap, the team narrows the universe down to roughly 80 and constructs a relative ranking table. The table ranks all shares based on their estimated expected returns. The portfolio manager is ultimately responsible for the stock position sizes, which generally reflect the following: 1. Potential upside of the stock; 2. The level of conviction in future earnings of the company; 3. Inherent risks associated with the stock/industry; 4. The portfolio exposure to macro variables such as currency, liquidity and country exposures; and 5. Any mandate or risk constraints
Buy and sell decisions are based only on the risk-adjusted expected return of a stock. The team buys with a high margin of safety and sells stocks as they approach fair value or there is a fundamental change to the investment case or upside potential. This results in a concentrated portfolio of the best investment ideas. Generally, the team is comfortable taking large position sizes in stocks with high levels of conviction in their valuation, irrespective of their position in the benchmark. The core equity funds, however, are constructed and managed to a client specified benchmark are therefore benchmark cognizant.

Team

The firm employs more than 290 permanent staff members in their various offices, with an experienced core investment team of over 60 people (portfolio managers, analysts, traders and economists). The firm is nearly 25% staff owned and senior staff have committed to owning shares for the duration of employment, which speaks to the alignment of their incentives with those of the underlying client. The majority of employees (57%) are Coronation shareholders and senior management runs the firm on a partnership basis.

The key individuals involved in the management of the equity strategy are CIO and lead portfolio manager Karl Leinberger and Co-portfolio manager Sara-Jane Alexander. Sarah Jane has been with the firm for 9 years, having started her career at JP Morgan Asset Management in London, as research analyst and co-manager of the UK Small Companies Fund. After 8 years with the firm, Karl Leinberger was appointed CIO at the time of Sarah joining. He continues to mentor younger analysts and manages the Balanced Plus Unit Trust. Coronation believes in a relatively flat management structure and regards long term broad ownership as a critical part of their success. From 2015 Coronation implemented a multi-counsellor approach, obviating the need for a specific back-up portfolio manager.

Product commentary

The South African long-only equity portfolio aims to deliver returns which are superior to a composite benchmark. The benchmark has been specified as 87.5% SA Equity (CAPI) + 12.5% international equity. The portfolio manager targets a 2% annual outperformance over the benchmark and the tracking error is limited to a 4-5% range.

In the last quarter of 2016, the firm solidified its positions in dual listed South African companies (Naspers, Steinhoff, BAT), based on the premise that these are still attractively valued, well diversified businesses with sound management teams. Exposure to food retailers and other consumer-facing businesses (Woolworths and Foschini) is light, and remains limited to companies where management has a sound track record of unlocking shareholder value. The portfolio's holdings in financials was up-weighted, based on their currently reasonable valuations and attractive dividend yields. Standard Bank, Nedbank and FirstRand have performed well.

Since its inception in 1996, the composite has managed to outperform the benchmark by 3.2% per annum.

Fees and costs

The Total Expense Ratio (TER), a measure of the actual expenses incurred by the fund over a 3-year period (annualised), includes the annual management fee. It comes to 1.28% for the portfolio and includes a 0.16% performance fee.   The Total Investment Charge (TIC) is 1.44%, and consists of the TER and the Transaction Cost of 0.16%

Discovery Equity Fund

ASISA Classification

South African - Equity - General

Firm

Discovery has mandated Investec Asset Management with the management of its building block portfolios. Investec Asset Management (IAM) is a wholly owned subsidiary of Investec Ltd and Investec Plc. Investec was founded in 1991 to provide a range of portfolio management services and products to both retail and institutional clients. In 1998 they launched a UK operation through the acquisition of Guinness Flight. Investec have established themselves as a successful firm with a 25-year history, with sizeable assets under management. The firm has grown largely organically, driven by a very stable senior management team led by the founder Hendrik du Toit. It is managed by an executive committee of five of the most senior people in the firm and who have been on the committee for the last seven years. Despite being wholly owned by Investec Plc, IAM is independently managed with limited intervention from the group. The firm has a strong reputation in the industry, both locally and globally.
A key development in the last three years was the sale of 15% equity of IAM to 40 of the most senior, loyal and significant contributors by its parent, Investec Plc. Senior employees have also secured an additional 4% over the next four years (after 1% was due in October 2016, a further 4% to be acquired by August 2020.)

As at December 2016, the firm had approximately R1 568 billion assets under management. The firm still has a predominantly institutional client base, representing circa 69% of assets while clients domiciled outside South Africa represent circa 82% of assets.
Investec, at the end of 2016, employed more than 170 investment professionals around the globe and had a BEE level 2 accreditation.

Philosophy and process

The Investec teams manage the Discovery building blocks in a manner which is consistent with the firm's overall investment philosophy and process. The Investec Asset Management (IAM) equity process is based on the firm's belief that it short-term inefficiencies and market anomalies result in mispricing of assets. Specifically, in the listed equity space, this is often reflected in changes in expectations of a company's future profits and cash flows, where investors can be slow to incorporate new information or are subject to behavioural biases. The General Equity strategy thus combines bottom up fundamental analysis with a top down view of the economic conditions and cycle.

This results in a fundamental focus on earnings revisions at reasonable value, but simultaneously incorporates an awareness of changes in momentum of economic cycle. Selection is driven by the following considerations: 1. Positive earnings revisions or knowledge that an upward revision is likely. This includes companies where their analyses leads Investec's analysts to believe that market/consensus forecasts are lower than company fundamentals merit. 2. Reasonable valuations, in terms of forward earnings and dividends, and improving profitability.

The top-down macro-thematic views are overlaid over the fundamental bottom up research. Both size and breadth of earnings revisions are monitored. In addition, a stock screening process identifies those companies trading at reasonable valuations as well as those with improving profitability ratios. From a bottom up perspective earnings revisions and valuations are therefore the key fundamental drivers over the long term of this part of the process. Investec acknowledge that equities and sectors can behave differently in various stages of economic cycle. The team have back-tested the SA stock market in order to create eight economic clusters or super-sectors. The team use their perspective on the broader economic cycle to assess the sustainability of earnings revisions and identify potential changes in future earnings ahead of the market. The super-sectors or clusters are: global cyclical (commodities), global cyclical (industrials), consumer defensive, SA consumer cyclical, infrastructure, gold, SA GDP services, global equity market beta.

Team

Rhynhardt Roodt is the lead portfolio manager on the General Equity Fund, ably supported by Chris Freund (joint co-head for the SA Equity and Multi-Asset strategies) and Grant Irvine Smith. The team has been together for more than ten years and their skill sets complement one another. Rhynhard is a specialist equity analyst and is responsible for driving the overall research agenda within the strategies. Grant has been extremely closely involved in the development and implementation of a proprietary stock selection model, which is used to construct enhanced index, active quant and market neutral strategies. The team also leverages off the analytical support of a broad SA equity analyst pool and has access to the global team of portfolio managers and analysts.

Product commentary

The Investec General Equity strategy tends to invest in liquid large capitalisation counters that meet their requirements of valuation and positive earnings revisions. Conviction is key to the strategy and therefore also benchmark agnostic. The fund is likely to be concentrated in large capitalisation stocks, with holdings of 25-35 names in the portfolio. The portfolio managers focus on absolute rather than relative return. While weights in portfolios will be driven by views on quality and conviction, large cap stocks can be held up to 10% and mid cap stocks up to 5%, reflecting underlying liquidity. The overall portfolio is continuously monitored for unintended sector bias or stock specific risk. Toward the end of 2016, the portfolio took some short-run pain from overweight holdings in Rand Hedges such as BAT and slightly underperformed the benchmark. The firm remains somewhat skeptical of Naspers, based on the belief that upward earnings revisions are increasingly unlikely as Tencent will find it difficult to beat current lofty consensus expectations. Positions in Sappi and Sasol have been consolidated, as both companies (based on fundamentals) are reasonably valued, but have potential pending upward revisions to earnings. Exposure to resources (in the form of diversified miner Glencore and Platinum counter South32) continued to contribute to performance, with commodity prices stabilizing. As such the team has trimmed slightly into strength.

Fees and costs

Expenses and costs for the Discovery Equity Fund are estimated to be in line with the Investec General Equity Strategies. The Total Expense Ratio (TER) is typically 2.06% which includes a performance fee of 1.08%. The portfolio incurs transaction costs of 0.60%, bringing the typical Total Investment Charge (TIC) to 2.66%.

Discovery Global Equity Feeder Fund

ASISA Classification

Global Equity General

Firm

Discovery has mandated Investec Asset Management with the management of its building block portfolios. Investec was founded in 1991 to provide a range of portfolio management services and products to both retail and institutional clients. In 1998 they launched a UK operation through the acquisition of Guinness Flight. Investec have established themselves as a successful firm with a 25-year history, with sizeable assets under management. The firm has grown largely organically, driven by a very stable senior management team led by the founder Hendrik du Toit. It is managed by an executive committee of five of the most senior people in the firm and who have been on the committee for the last seven years. Despite being wholly owned by Investec Plc, IAM is independently managed with limited intervention from the group. The firm has a strong reputation in the industry, both locally and globally.

A key development in the last three years was the sale of 15% equity of IAM to 40 of the most senior, loyal and significant contributors by its parent, Investec Plc. Senior employees have also secured an additional 4% over the next four years (after 1% was due in October 2016, a further 4% to be acquired by August 2020.)

As at December 2016, the firm had approximately R1 568 billion assets under management with the Investec SA Value Equity portfolio representing just over R18.4 billion. The firm still has a predominantly institutional client base, representing circa 69% of assets while clients domiciled outside South Africa represent circa 82% of assets.

Investec, at the end of 2016, employed more than 170 investment professionals around the globe and had a BEE level 2 accreditation.

Philosophy and process

The Investec teams manage the Discovery building blocks in a manner which is consistent with the firm's overall investment philosophy and process. The global team applies the so-called 4Factor process to the global feeder funds. The Investec Asset Management (IAM) equity process is based on the firm's belief that short-term inefficiencies and market anomalies result in mispricing of assets. The 4Factor investment process has been designed with the aim of finding mispriced opportunities in a consistent, repeatable manner and within a disciplined approach.

The 4Factor team believes that share prices are driven by four fundamental factors over time. Empirical research and testing, academic study and intuitive reasoning have lead the team to identify four sets of characteristics: Strategy, value, earnings and technicals. High quality companies with effective management teams, where stocks are trading at a discount to fair value, but with strong dynamics and momentum (upward earnings revisions and share price momentum) are likely to not only generate alpha, but do so in a stable manner.

The first step of the 4Factor process entails narrowing down the universe, using an objective proprietary screening model to systematically score and rank all the companies based on the four investment criteria. Each factor receives a score between one and four, and a short list of potential good ideas is compiled from the top tier (typically about 160, of which 135 are selected). The team does fundamental bottom-up research on each of the good ideas – which entails an in-depth analysis of the key issues that will drive stock prices - and the designated analyst formulates an investment case. The case is presented to and debated by the broader team. If the case can be made that sentiment has been overly negative, and shares are therefore trading below their intrinsic value, the company may make it onto the buy list. Conversely, a sustained upward trend in share-prices can also prompt a closer look, as the firm finds that behavioural biases tend to persist. The bottom up research, combined with a top-down macro-thematic view, allows the designated global analyst to form a view of the relative value of a share. Excessive noise from cyclical trends (purely momentum driven, not fundamentally justified) are avoided by using normalised EBITA measures. The team can subsequently assess what the upside is (the extent of and likelihood that earnings will be revised upward, or stock prices appreciate). A 'best idea' generally requires 50% upside. A predetermined review price - a measure of the change in the valuation that will bring a stock to fair value – acts as a trigger for reassessing a stock's position or weight.

The portfolio manager would decide to sell or trim a position if the company has reached its review price and the analysts cannot find upside to justify continuing to hold the position; a new opportunity arises which demonstrates a potential for greater upside than the current position or if the position breaches any of the predetermined risk limits.

Team

James Hand, lead portfolio manager for the fund, Co-head of 4Factor Equities and Co Chief Investment Officer has more than 20 years industry experience and has been with the firm since 2000. Prior to joining Investec, James spent time at Schroder Investment Management, specializing in small cap technology stocks. Whilst at Investec, he has covered a range of global sectors and has been the lead author and developer of the 4Factor process. Mark Breedon, himself a seasoned industry player of more than 40 years, supports James in his role as Co-Head of 4Factor equities. Mark has been managing global equity for Investec for the past 13 years, having joined Investec in 2003 from Alliance Capital Management. While at Alliance he managed the USD500 million Worldwide Privatisation Fund and the NYSE listed Southern Africa Fund and previously managed developed market equity accounts for Brinson Partners. Mark and James are supported by the broader 4factor team and draw on the wealth of experience of the strategy leaders for the Global Endurance, Global Dynamic, Emerging Markets and Asian strategies. The designated global analyst for each super-sector helps to ensure that the portfolio manager (James Hand for the Global Core Equity strategy) has a sufficiently-nuanced view of the individual stocks to be selected for the portfolio.

Product commentary

The Feeder Funds are Rand denominated funds which aim to give investors dedicated international market exposure, but at a lower level of risk (and at lower cost) than with direct offshore mandates. The majority of the Discovery Global Equity Fund's exposure is in developed markets such as the US, UK, Europe and Japan. The portfolio underperformed the MSCI during much of 2016, mainly due to the defensive nature of the strategy in a risk-on environment. The team was hesitant to trim UK exposure into weakness and has therefore maintained a fairly substantial exposure, on expectations that Brexit will be less painful than doomsayers predict. While the firm expects that the Fed will normalize interest rates gradually, this is likely to add to short run volatility and de-rating of price to earnings ratios. Defensive positions in quality stocks, while experiencing some initial pain, are likely to prove resilient in the still uncertain global environment.

Fees and costs

Expenses and costs for the Discovery Global Feeder Funds are estimated to be in line with the Investec Global Franchise Strategies. The Total Expense Ratio (TER) is typically 2.09% which includes an annual management fee of 1.75%. The portfolio incurs transaction costs of 0.01%, bringing the typical Total Investment Charge (TIC) to 2.10%.

Discovery Global Real Estate Feeder Fund

ASISA Classification

Global Property

Firm

Discovery has mandated Investec Asset Management with the management of its building block portfolios. Investec was founded in 1991 to provide a range of portfolio management services and products to both retail and institutional clients. In 1998 they launched a UK operation through the acquisition of Guinness Flight. Investec have established themselves as a successful firm with a 25-year history, with sizeable assets under management. The firm has grown largely organically, driven by a very stable senior management team led by the founder Hendrik du Toit. It is managed by an executive committee of five of the most senior people in the firm and who have been on the committee for the last seven years. Despite being wholly owned by Investec Plc, IAM is independently managed with limited intervention from the group. The firm has a strong reputation in the industry, both locally and globally.

A key development in the last three years was the sale of 15% equity of IAM to 40 of the most senior, loyal and significant contributors by its parent, Investec Plc. Senior employees have also secured an additional 4% over the next four years (after 1% was due in October 2016, a further 4% to be acquired by August 2020.)

As at December 2016, the firm had approximately R1 568 billion assets under management with the Investec SA Value Equity portfolio representing just over R18.4 billion. The firm still has a predominantly institutional client base, representing circa 69% of assets while clients domiciled outside South Africa represent circa 82% of assets.
Investec, at the end of 2016, employed more than 170 investment professionals around the globe and had a BEE level 2 accreditation.

Philosophy and process

The Investec teams manage the Discovery building blocks in a manner which is consistent with the firm's overall investment philosophy and process. The global team applies the so-called 4Factor process to the global feeder funds. The Investec Asset Management (IAM) equity process is based on the firm's belief that short-term inefficiencies and market anomalies result in mispricing of assets. The 4Factor investment process has been designed with the aim of finding mispriced opportunities in a consistent, repeatable manner and within a disciplined approach.   The Global Real Estate Securities Fund is a sub fund of the Investec Global Strategy Fund, which is run consistently with the firm's overall multi-asset approach, spanning equity and fixed income as well as real estate and cash.

The 4Factor approach remains the overarching theme, though with nuances adjusted for the property market. The overall 4Factor approach is based on the premise that share prices are driven by four fundamental factors over time. Empirical research and testing, academic study and intuitive reasoning have lead the team to identify four sets of characteristics: Strategy, value, earnings and technicals.   High quality companies with effective management teams, where stocks are trading at a discount to fair value, but with strong dynamics and momentum (upward earnings revisions and share price momentum) are likely to not only generate alpha, but do so in a stable manner. Within the property sector, valuation is seen as the key driver in the decision-making process. The team employs a dividend yield valuation methodology, where the fair value yield and the one and two year exit yield are determined taking into account the growth prospects of the company, and complements this with fundamental measures, such as the quality of the underlying assets, the track record of the management team, critical mass (size of portfolio), liquidity and any other stock specific information.
The firm follows a five stage process to reach a buy/sell list for the property strategy: Stage 1 is a top down analysis of the economic conditions and the industry. Stage 2 comprises individual company risk assessments. Companies are assigned a score from 1 to 4, based on a number of factors. These include the quality of assets, management track record, critical mass (is a portfolio big enough to be self-sustaining and continue growing), liquidity, debt and levels of gearing and distribution growth forecasts. The 3rd stage consists of individual company valuations, relative to the company's own fundamentals. The 4th stage distils the process into a portfolio of best investment ideas. This is driven by the relative attractiveness of each stock in comparison to its peers and taking some macro-economic factors (e.g. forecast bond yields) into account. Stage 5 consists of portfolio construction: Risk assessments identify company specific and portfolio risks (ranging from liquidity to correlation), which are used to adjust benchmark weighting and arrive at an appropriate active weight.   Pending corporate actions or legislative changes may be additional factors which are considered when making these adjustments. The proprietary relative valuation model ranks all the stocks in the universe according to the relative forecast total return (relative to the listed property index, the FTSE EPRA/NAREIT Global TR USD) using 1 and 2-year projections.

Maximum weightings are initially based on the model portfolio, but active weights are adjusted as opportunities arise or per mandate restrictions.

The higher the relative total returns compared to the benchmark and the lower the company risks, the higher the positive active weights. However, the team typically would not hold more than 10% in any one stock. The firm is also able to invest in off-market opportunities. These are at times brought to the team's attention due to their established and extensive industry contacts, including those facilitated by an established market presence in Australasia and the UK. Off-market opportunities go through rigorous due diligence.

Team

The Investec Global Real Estate Securities Fund is a sub fund of the Investec Global Strategy Fund, which is under the leadership of Phillip Saunders and Iain Cunningham. Phillip is also the Co-Head of Multi-Asset Growth Strategies and portfolio manager for the total return, global multi-asset and protected strategies. His career spans more than 20 years and he was the founding director of Guinness Flight Global Equity Director, acquired by Investec in 1998. Iain, a PM with the Multi Asset team, started his career at Schroders, where he was the lead fund manager of the Schroder ISF Global Multi-Asset Fund. In line with the firm's specialist multidisciplinary approach, however, the real estate sleeve is managed by Neil Stuart Findlay and Peter Clark. Neil Stuart Findlay joined the SA Equities and Multi Asset team as portfolio manager in 2004, after a stint in London as project manager and analyst in the trade implementation team. He has been in the industry for more than 18 years, finding his start with Coutts Private Bank and Deutsche Asset Management in the UK. His current role within the Multi-asset team sees him focus on listed property and he is supported by the broader analyst team. Peter joined the Investec Property Group as analyst in 2009, before acting as the Sector Head of Property until May 2015 and becoming a portfolio manager within the multi-asset team. The co-managers focus on listed property and are supported by the broader analyst team.

Product commentary

The Feeder Funds are Rand denominated funds which aim to give investors dedicated international market exposure, but at a lower level of risk (and at lower cost) than with direct offshore mandates. The Discovery Global Real Estate Feeder Fund holds units in the Investec Global Real Estate Securities Fund, which is itself a sub fund of the Investec Global Strategy Fund. The portfolio underperformed the FTSE EPRA/NAREIT Developed TR USD over the last quarter of 2016, as defensive asset classes fell from favour in a risk-on environment. The portfolio has also been under pressure from its exposure to under-pressure UK companies, but the manager has been loath to sell into weakness. The recent uptick in UK construction is looking promising and the manager is likely to capitalise on a still relatively weak pound with quality property investments available at depressed valuations.

Fees and costs

Expenses and costs for the Discovery Global Feeder Funds are estimated to be in line with the Investec Global Franchise Strategies. The Global Real Estate Feeder Fund is invested in the Investec Real Estate Securities Fund, in turn a sub-fund of the Investec Global Strategy Fund, a Luxembourg domiciled SICAV. The ongoing charge is typically 2.08%.

Discovery Money Market Fund

ASISA Classification

South African - Interest Bearing Money Market

Firm

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A key development in the last three years was the sale of 15% equity of IAM to 40 of the most senior, loyal and significant contributors by its parent, Investec Plc. Senior employees have also secured an additional 4% over the next four years (after 1% was due in October 2016, a further 4% to be acquired by August 2020.)

As at December 2016, the firm had approximately R1 568 billion assets under management. The firm still has a predominantly institutional client base, representing circa 69% of assets while clients domiciled outside South Africa represent circa 82% of assets.

Investec, at the end of 2016, employed more than 170 investment professionals around the globe and had a BEE level 2 accreditation.

Philosophy and process

The Investec teams manage the Discovery building blocks in a manner which is consistent with the firm's overall investment philosophy and process. The Money Market strategy's first priority is capital preservation, with an active approach based on the following underpin: fair value is determined by economic fundamentals, and yields will revert to fair value over time, the existence of segmentation, asymmetric information and a small number of market participants created opportunities along the yield curve, which the firm can identify and exploit, based on their fundamental research.
The strategy invests in a range of South African money market instruments, including bankers' acceptances, debentures, negotiable certificates of deposit, treasury bills and call accounts. The investable universe is limited to maturities of less than one year and duration of no more than 90 days. This ensures that the underlying issuers pose little default risk.

The team is very conscious that liquidity is a prime concern, and the issue is addressed by a) limiting the investable universe to negotiable instruments (i.e the manager can adjust the duration if the interest rate environment changes) and b) ensuring that the call account has adequate funds to redeem cash at short notice when necessary. The money market portfolio, as with the firm's other strategies, leverages off the broader analyst resource base and is driven by fundamental research. A macroeconomic analysis is used to generate forecasts of key economic variables. The projected returns from the proprietary process, as well as those based on published consensus, are used to forecast inflation for the next year. Likely prime rate scenarios are subsequently formulated and used as primary input in the money market optimisation model. The model generates a set of 3-month yield curve forecasts, which informs the gradient of the forward money market yield curves are derived. The team use it to generate a return matrix and set a strategic duration. This is similar to the setting of a strategic asset allocation. The tactical part focusses on taking advantage of short term trading opportunities and exploiting market inefficiencies. This is similar to the first and third stages in the firm's implementation of the balanced strategies. The credit decision is a systematic and replicable process, which allows the firm to identify the appropriate sizing and direction of any adjustments to duration or yield curve positioning. It involves:
• an initial assessment and pre-screening, the decision on whether to analyze more closely is taken here
• Fundamental analysis and due diligence
• Credit Committee approval
• Pricing and investment decision, which includes the in-house valuation of present opportunities
Once an instrument is included in the portfolio, the team undertakes ongoing monitoring.

Team

Lisa MacLeod is the lead portfolio manager for the Money Market fund, a natural extension of her role within the SA Rates team as manager for the short duration strategies. Vivienne Taberer, investment specialist and portfolio manager in the Emerging Markets Fixed Income team (which also analyses South African credit) supports Lisa as analyst and portfolio manager. Both managers gained experience and exposure to complex credit markets during periods of employment at large asset management firms/investment banks in London (e.g. SBC Warburg, Standard Bank and Mizuho International) before joining Investec.

Product commentary

The strategy's first priority is capital preservation, but the aim remains to earn a higher level of income than fixed and call deposits. During the fourth quarter of 2016, floating rate notes were at elevated spreads and the team continued to add to its exposure to longer dated maturities. The traditionally cash-tight December period saw the fund hold more short-dated instruments and detracted slightly from the annual performance. The fund nonetheless managed to outperform the STeFi by 20bps in the last quarter of 2016. The team continues to look for opportunities to add duration and remains selective on levels within an environment of fairly stable local interest rates, coupled with global uncertainty.

Fees and costs

Expenses and costs for the Discovery Money Market fund are typically a 0.58% TER and TIC.

Fairtree Met Equity Fund

ASISA Classification

South African - Equity - General

Firm

Fairtree Capital was launched by Andre Malan in 2003. The first fund (The Fairtree Capital Fund) was part of a suite of funds managed by Decillion Fund Management (DFM), but the management team of Andre Malan, Kobus Nel and Bradley Anthony purchased the business from DFM in 2006 to set up an independent firm. Fairtree Capital started off as a hedge fund business, but has expanded through a number of strategic partnerships into a multi-strategy fund management business. In 2010 Stephen Brown joined the business and launched a directional-biased Long Short Equity Fund. The Assegai business unit launched the Fairtree General Equity Fund in 2011 and the Volatility Arbitrage and Fixed Income Credit teams joined Fairtree in the same year.

The firm's client base is predominantly made up of institutional investors with a significant asset boost when the Norges Investment Management Bank (NBIM) invested in the Long Only Equity strategy. More than 70 % of AUM is managed in long only mandates with hedge funds making up the remainder. The firm had more than R 29 billion in assets under management at the end of 2016.

The Directors (Andre Malan, Kobus Nel and Bradley Anthony) own 100% of the company shares, but ownership of business units is shared with senior portfolio managers. Each of the business unit's interests are therefore aligned through their equity shareholding and the profit-sharing arrangement.
The firm (at December 2016) was in the process of applying for its BBEEE certificate.

Philosophy and process

The investment philosophy of the Fairtree Capital equity team is firmly anchored in the following beliefs: firms with inherent superior cash flow generation ability tend to outperform the market over time and often become industry leaders in their markets. Over time, high quality management teams are able to grow shareholder value by allocating excess cash to growth opportunities. The growth potential that this brings is often overlooked by the market. Mispricing provides opportunities to invest in future growth. Also, the team believes that the cash flow generating ability of these firms can be influenced by prevailing economic conditions and appreciate the potential risk that cycles can last longer than many investors expect. This informs and broadens thinking on both stock selection and portfolio construction.
The team has a flexible and pragmatic investment style and will move between value and growth styles as and when either becomes more appropriate (blended). The philosophy and approach is likely to lead to a quality bias in the portfolio over time.

Fundamental research and analysis is completed on a universe of, on average, the top 80 companies of the JSE by market cap. This fundamental process entails careful evaluation of each potential opportunity, based on components of shareholder returns such as ratings (valuation), earnings and dividends. The team then investigates internal and external drivers that could lead to excess return. This allows the team to find either a growth or value underpin. Philosophically the team will tend to look for either a growth or value underpin in large and mid-cap stocks, while they would favour value opportunities in the small cap space (<R10bn). From a valuation point of view, a very high margin of safety is required for companies with cyclical and unpredictable cash flow streams, while a low margin of safety is acceptable for leading companies in attractive industries where cash flows are reasonably stable and predictable. Growth shares that appear expensive on a forward price/earnings (PE) basis are considered investable, if the team believe the market is underestimating the near term growth potential. The portfolio is constructed using a combination of investment strategies depending on prevailing macro-economic and financial market conditions. The resulting views will determine which strategic focus area will be favoured and how capital will be allocated based on various investment strategies including Yield, Defence, Value, Earnings Growth, Low Quality, High Quality and Macro Momentum.

The investment process results in a well-diversified portfolio of between 40-60 stocks. This takes account of stock limits between 0 and 10% as well as sector weightings, with due cognizance of sectors which are driven by similar underlying profit drivers (e.g. interest rate sensitivity). The fund managers prefer a number of smaller positions (with weightings between 2 and 4%), rather than a few large positions of 8% - 10%. While the team invest across the market cap spectrum, there is a preference for more liquid large and mid-cap counters. Small cap positions will only be entered into where it is possible to fully exit within one month. The portfolio tends to be fully invested with typical cash levels between 1-2.5%. The exception would be periods of market turmoil and crises during which time cash levels around 10% and above could be held.

Team

Portfolio managers Stephen Brown and Cor Booysen are seasoned investors, who have experienced different market cycles and conditions. While Cor Booysen only joined Fairtree Capital in 2013, he worked with Stephen at RMB Asset Management between 2007 and 2011. They are co-portfolio managers, which mitigates against key-man risk. Both portfolio managers have a strong knowledge of the resources sector, which is particularly helpful in a South African context. They are supported by an expanding team of analysts, which has grown in both maturity and in its reach across the business units. The firm is continually expanding its skills base, with a number of new hires in the past 6 months. This includes younger analysts and experienced individuals: Cephas Dube and JP Verster, both with 10 years of experience, joined as portfolio managers in 2016, Amy Petersen and Anne-Marie Gous (9 years' experience) joined as Institutional Client Specialist and Business Development Consultants, with a view to ensure that key investment professionals remain focused on their core competencies. Each business unit has full autonomy in hiring and investment decisions. The firm ensures that incentives are aligned by linking bonuses (including those of the research analysts) to fund performance.

Product commentary

The Fairtree Met Equity fund has managed to consistently outperform its benchmark (the FSTE/JSE SWIX), with an average annualised outperformance of 3.34%.

Recent performance has been boosted by an uptick in commodity prices, as the fund held substantial positions in Kumba, Impala, Anglo and diversified miners BHP Billiton. The fund maintains an overweight in selected strategic sectors, those with an earnings growth focus include consumer discretionary firms with resources positions to take advantage of cyclical plays while financials and consumer discretionary firms are favoured for their value and yield propositions.

Fees and costs

The Total Expense Ratio (TER) for the fund is 2.5%, including an annual management fee of 1.14% and a 15% performance fee. Transactions costs of 0.53% contribute to the Total Investment Charges (TIC) of 3.03%.

Investec SA Value Equity Fund

ASISA Classification

South African - Equity - General

Firm

Investec Asset Management (IAM) is a wholly owned subsidiary of Investec Ltd and Investec Plc. Investec was founded in 1991 to provide a range of portfolio management services and products to both retail and institutional clients. In 1998 they launched a UK operation through the acquisition of Guinness Flight. Investec have established themselves as a successful firm with a 25-year history, with sizeable assets under management. The firm has grown largely organically, driven by a very stable senior management team led by the founder Hendrik du Toit. It is managed by an executive committee of five of the most senior people in the firm and who have been on the committee for the last seven years. Despite being wholly owned by Investec Plc, IAM is independently managed with limited intervention from the group. The firm has a strong reputation in the industry, both locally and globally.
A key development in the last three years was the sale of 15% equity of IAM to 40 of the most senior, loyal and significant contributors by its parent, Investec Plc. Senior employees have also secured an additional 4% over the next four years (after 1% was due in October 2016, a further 4% to be acquired by August 2020.)

As at December 2016, the firm had approximately R1 568 billion assets under management with the Investec SA Value Equity portfolio representing just over R18.4 billion. The firm still has a predominantly institutional client base, representing circa 69% of assets while clients domiciled outside South Africa represent circa 82% of assets.
Investec, at the end of 2016, employed more than 170 investment professionals around the globe and had a BEE level 2 accreditation.

Philosophy and process

The Investec Value team and portfolio manager John Biccard, believe that market inefficiencies can cause valuation anomalies. This can lead stock prices to deviate from fair value, even for protracted periods of time. Six principles guide their philosophy: 1. Bottom up stock picking - Investec believe bottom up fundamental analysis adds more value than macro forecasting as forecasts can be made with more certainty. As such the focus is on investing in companies with little awareness of benchmarks. 2. Only buy companies that you understand 3. Avoid stocks with high historic valuations, never buy a stock on a normalised Price Earnings (PE) ratio over 25x. 4. Dividends count - Long term dividend policies and forward looking yields are a critical part of the stock selection process. A consistent dividend policy provides a stable underpin to a steady income stream. 5. Buy real assets - real assets perform better than intellectual capital assets over the long-term and real assets are considered more reliable for minority investors. 6. Beware of fads and fashions (stocks and sectors).

The principles translate into a decidedly contrarian portfolio, with a deep value bias. Portfolio construction is a bottom-up valuation-driven exercise. The absolute weight of any stock depends in the conviction of the portfolio manager, market capitalisation and liquidity profile of a company. In general, positions in large cap stocks (greater than R5bn market cap) are limited to 10% of the portfolio and 5% for those below the R5bn market capitalisation mark. These limits may however be exceeded during periods of extreme market conditions. The team puts a lot of focus on a disciplined sell process. When a stock reaches its target price, it is sold. Valuation criteria (PE relatives, Price to Book, Dividend Yields inter alia) are supplemented by technical analyses, which help the team to identify unloved stocks.

Team

Alistair Mundy heads up the Value team for the firm, but the local SA Value Equity strategy is under the stewardship of John Biccard. John, before joining Investec as Sector Head of Industrials in 2000, worked at HSBC (then Simpson McKie Stockbrokers) as a rated analyst, before achieving Directorship. John leverages off the analytical support of an SA equity analyst pool of just over 10 people. The four portfolio managers (and seven analysts) from the global value team also provide a useful sounding board. Portfolio Manager John Biccard's views and experience however, remain very much the driving force behind the portfolio. The firm has recently appointed Andrew Joannou as a portfolio manager for the Value team, partly with a view to provide back-up for John. Andrew brings sixteen years of experience to the table.

Product commentary

The Value Fund aims to provide long term capital growth by investing in unloved, contrarian stocks which are trading below their intrinsic market value. This strategy, during a period in which momentum carried the stock market, experienced a significant amount of mid-term pain. However, 2016 proved a significant turning point. Spurred by a resource and commodity rally, the fund saw a return of more than 50% over the course of 2016 (January to December). Based on the since inception (1997) annualised return of 20.1%, the long term value proposition appears to hold true. Going into 2017, the fund has maintained its large overweight positions in Basic Materials (60% of the portfolio) and resource counters such as Impala Platinum (10%) and AngloGold (9%).

Fees and costs

The Total Expense Ratio (TER) for the Investec Value Fund is 2.24%, which includes a performance fee of 1.04%. The portfolio incurs transaction costs of 0.25%, bringing the typical Total Investment Charge (TIC) to 2.49%.

Nedbank Rainmaker Fund - Abax Investment Managers

ASISA Classification

South African - Equity - General

Firm

Nedgroup has mandated the team at Abax Investments to manage the Nedbank Rainmaker Fund. Abax Investments (formerly Polaris Capital) was founded in 2003 as a boutique asset manager and remains an owner managed entity. Abax staff and three charitable trusts own approximately 75% of the equity and retain 100% voting rights, while the remaining 25% is owned by AMG, a global asset management company with interest in boutiques worldwide. It is worth noting that Nedgroup remains a longstanding and significant relationship, with Abax managing a number of sub advised accounts. The Nedbank Rainmaker Fund makes up about 17% of the firm’s AUM (at 30 September 2016).
Assets under management as at January 2017 amounted to R86 billion. The firm has clear ambitions to grow existing mandates through performance, rather than mere asset gathering. The client book has shown healthy growth, with a majority of institutional clients (just over 70%). Equity remains a core part of the Abax business, but balanced mandates have recently gained momentum and the firm is looking to expand its hedge fund and fixed income reach. The original owner-manager team retains control and the team regard AMG as a hands-off partner, with the potential to continue to enhance the firm’s global reach.

Abax is rated a level 3 contributor to B-BBEE and continue to improve their overall score year on year.

Philosophy and process

Abax believes that markets are inefficient and therefore valuations are not always fully reflective of the true worth of a company. They attempt to identify companies which are therefore undervalued, with an emphasis on those with superior dividend and earnings growth prospects. While they are hesitant to pigeonhole their style, the result tends to be a relative value approach, with a focus on stock-picking and a bias toward high quality businesses. Fundamental research forms the basis of the investment process. As a starting point, the team aims to build an understanding of each company, which company fundamentals currently drive its earnings prospects and what macro factors may contribute to its future prospects. While a top down perspective is therefore added, the process is fundamentally driven by bottom-up stock picking. The firm uses a combination of in-house models and broker research to inform their analyses and conducts more than 200 company visits and management interactions per year.

It is worth noting that this slightly contrarian/out-of-the box approach has resulted in a predominantly benchmark-agnostic view. The firm, however, is benchmark cognizant and manages portfolios such as the Rainmaker Fund to a specific benchmark. But the bottom-up assessment of investment merits remains the fundamental starting point. Portfolio positions are not built around a benchmark weight plus or minus a specific percentage, but reflect the level of conviction of the team (taking into account any mandate constraints).

The level of conviction is informed by a ranking table, which is updated on a daily basis. It is a record of around 140 stocks, containing the key stock metrics which drive valuations. The process will result in a high conviction portfolio, covering a fairly concentrated selection of companies. A high conviction position may have an 8 to 10% weighting in the portfolio, but the team have no qualms about not holding a stock if they do not like the investment case. While portfolio managers have individual accountability, portfolios may differ in position sizing or at the margin.

The firm outsources non-key functions to recognized partners, allowing the core team to focus on their value-adding investment functions.

Team

Abax have grown to a staff complement of 19 people (as at December 2016), with an additional two trainees on two-year contracts.

The core investment team, including the founding members, has been together for a number of years with newer team members added organically. Great care is taken in the hiring processes. The initial focus was on hiring experienced members, who would add specific complementary skills to those of the founding members. Omri Thomas, Steven Minnaar and Wallie van der Walt joined between 2006 and 2009, while Rashaad Tayob brought his fixed income experience to the team in 2012. The more recent hires have added to the firm's multi-asset, fixed income and global capabilities: Matthew de Wet was appointed as Portfolio Manager (Multi-Asset) in November 2015, bringing 16 years investment experience (including experience at Nedgroup) and Adam Spagnoletti and Dylan Oelofse joined in December 2015 as Assistant Portfolio Managers (Global Equity and Fixed Income respectively). The team now consists of nine investment managers, who are the primary decision makers and supported by the team of analysts and the trainees. Justin Hollis and Marius van Rooyen are the lead Investment managers on the FINDI mandates, whereas Anthony Sedgewick is the lead manager on the SWIX mandate. Steve Minnaar is the Head of Equity Research and runs the investment team's weekly investment meetings.

Staff receive a fixed salary, but all permanent staff are shareholders in the company, receiving quarterly dividends dependent on the financial performance of the company. Trainee analysts earn a performance related bonus, which therefore also ensures that they share in the profitability of the strategies and the business.

Product commentary

The South African long-only equity portfolio aims to deliver returns which are superior to a composite benchmark (ALSI as at December 2016, but subject to change). The experienced team applies its fundamental bottom-up stock picking approach and builds a portfolio which is suitable for investors who are aiming to achieve maximum capital appreciation over the medium (5-7) term. As the portfolio is fairly concentrated and consists of high conviction, appetite for risk tends to be mid-to-high. Volatility has been slightly below the benchmark over the 5-year horizon. The firm's emphasis on long-run relative value has seen it maintain its fairly substantial holdings in diversified Industrials and Rand Hedges such as BHP Billiton, Mondi and BAT. Naspers too remains a key position, albeit below benchmark (ALSI). The holding (just over 15%) reflects a cognisance of benchmark risk and concentration risks, but is primarily based on the team's assessment of the long-run value that can still be unlocked (mainly driven by Tencent).

Fees and costs

The Total Investment Cost (TIC) for the Rainmaker Fund is the Total Expense Ratio (TER) (service fee + performance fee + VAT) and any transaction costs. The TIC is 1.92% for class A – with 0.19% transaction cost, and TER of 1.73% (including the annual management fee of 1.5%).

Prudential High Yield Domestic Bond Fund

ASISA Classification

South African - Interest Bearing - Variable Term

Firm

Prudential Plc was founded in 1848 and is one of the world's largest financial services companies. Prudential is now an international group operating across Europe, America, Asia and Africa with more than £457 billion under management at the end of 2016. Prudential Portfolio Managers (South Africa) (Pty) Ltd was established in 1994 and is the holding company for all of Prudential's entities in South Africa. On 1 July 2014, Prudential Portfolio Managers (South Africa) (Pty) Ltd created a new subsidiary company, Prudential Investment Managers (South Africa) (Pty) Ltd (Prudential South Africa). Prudential South Africa became the new responsible asset manager at the time.

49.99% of Prudential Portfolio Managers (South Africa) (Pty) Ltd is owned by M&G Investment which in turn is wholly-owned subsidiary of Prudential Plc. 28.01% of ownership of the South African company vests in the Prudential Staff Investment Company ("NewCo") benefitting the employees of Prudential and a further 22% of the business is owned by the Thesele Group, a BEE consortium.

Prudential have continued to grow the business with assets under management in excess of R213 billion as at December 2016. This includes institutional and retail assets.

Prudential is a Level 2 BEE contributor.

Philosophy and process

Prudential can be categorised as a value investor that operates with a pragmatic framework. They believe markets are broadly efficient over long periods of time, but that mispricing happens over shorter periods of time. The team therefor search for investments they believe are being mispriced in the market relative to their fundamental value and hence likely to deliver outperformance over time. Prudential believes that value investing, in a bond environment, means that corporate debt is particularly attractive. The focus on credit bonds has evolved alongside the evolution of the South African credit market since the 2000s. The strong risk control culture, combined with value investing, fits in well with the firm's overall low risk philosophy. The investment philosophy also reflects the natural process of skills-transfer from major UK shareholder M&G, who have one of the largest credit teams in the UK.
Next, each opportunity is systematically assessed to see whether it can be translated into excess returns over the medium term. To confirm a specific corporate bond's yield represents a real value proposition. The team uses Prudential's Global Credit Risk Model for this. It builds on the first step, in evaluating the underlying fundamentals of the issuing company according to the following guiding principles:

- Who is the borrower and what is the debt funding?
- How will the repayment be funded? Primary or secondary sources may include cash flow profits, sales of assets/business or refinancing
- What risks can jeopardize repayment? Risks are related to industry, commercial viability, management and shareholders, sales and profitability, investment decisions, funding/financing decisions, debt structures.
- How is the debt facility structured to protect investors' interests?

The credit analysts will present their findings to the Credit Committee. A time-specific and time-dependent target price is set for the initial purchase (pricing is continually reassessed). Once a bond has been selected for purchase, bids are submitted at the minimum target spread. The team will opportunistically up-weight exposure if allocations can be obtained at a higher spread. Thirdly, risk controlled portfolios are constructed in line with the firm's overall philosophy of maximizing upside potential and controlling downside risk. The portfolios are constructed in a team environment, which means that there is a peer review and active debate around each decision. The asset allocation and credit committees drive the process, using the investment meetings and daily morning meetings as forum. Assets are invested in credit issues first. The team considers risk controls and liquidity and prefers holding a number of smaller bets rather than a few concentrated ones. Maximum exposure to any one instrument will generally be 1.5% and 4% for any one issuer. Once the credit positions have been filled to the level of credit exposure which the team has targeted, government bond purchases are used to achieve the appropriate overall duration position in the portfolio. The final step of the investment process consists of regular monitoring to ensure that portfolios comply with mandate and risk parameters.

The various risk factors measured include:
• Duration, yield curve and convexity risk – considered against the benchmark and in light of recent market activity and shifts in the yield curve. The team looks at yield buffers available for bonds of different maturities, versus cash.
• Spread risk – inherently the credit process will address this, as higher value issues are favoured, but the team also looks at the spreads in other similar peer group markets.
• Liquidity risk – a cash and relatively liquid government bond component addresses liquidity concerns
• Default risk – the firm prefers to take smaller positions across a wide range of issues and issuers. The maximum exposures will be 1.5 and 4% to issue and issuer respectively.
Portfolios are continuously monitored and controlled to ensure that they deliver to their mandate within risk tolerances. Client limits typically involve ratings based restrictions and constraints on duration and asset class.

Team
Prudential South Africa employs 166 people including 66 operational staff. Prudential follow a team based approach, with the asset allocation and credit committee driving the process. Highly experienced CIO David Knee (26 years in the industry and 19 with Prudential) is at the helm of the strategy, alongside Fixed Income portfolio manager Gareth Bern (12 years with Prudential). They are assisted in the implementation of their Fixed Income strategy by Anna Germanis, who has more than 17 years trading background. The Fixed Income team is in close contact with their international colleagues. The team leverages off the capabilities and experience of their international peers from M&G and members from both teams have at times been on secondment to their counterparty teams, adding to the breadth of their market experience and exposure.

Product commentary
This fund aims to maximize the income from a relatively steady asset base, by actively investing in a diversified portfolio of South African high-yield bonds (government, semi government and corporate bonds). The High Yield Bond Fund delivered a total return of 0.33% in the fourth quarter of 2016, for a total return of 15.4% for the year, which is in line with the benchmark (the BEASSA All Bond Index). The team took advantage of the post-Trump nerves and knee-jerk sell-offs to add duration to the fund. As bond yields rallied throughout 2016, being long duration has stood them in good stead.

Fees and costs

The Total Expense Ratio (TER), showing the charges, levies and fees relating to the management of the portfolio (calculated on a rolling three year basis, annualised) for the A-class portfolio is 0.9%, while Transaction Costs of 0.05% are incurred. The Total Investment Charges (TIC) therefore come to 0.95%.

Sesfikile BCI Property Fund

ASISA Classification

South African - Real Estate - General

Firm

Sesfikile Capital was started in 2010 as a company with a dedicated focus on the South African listed property sector. The Unit Trust fund (the Sesfikile BCI Property Fund) was launched in November 2011, shortly after the firm's inception. Founding members, Evan Jankelowits, Mohammed Kalla and Kundayi Munzara, share a passion for the sector and are still at the helm as directors of the company and as core investment team. The company's assets under management have grown from circa R1.5 billion at inception to just short of R16 billion as at January 2017. Assets comprise predominantly South African institutional clients (86%), with 8-9% of AUM from Global Institutional and Retail clients (6.5% and 2% respectively).

Towards the end of 2016, a decision was taken that Royal Investment Managers could acquire a 25% stake in Sesfikile Capital. The Royal Bafokeng holds 50% shares in Royal Investment Managers, with the remaining 50% ownership split 35:15 between RMI and management. Sesfikile Capital's shareholding structure as at January 2017 was 25.01 % Royal Investment Managers; 37.49% Ukukhula Sibanye En Commandite Partnership and 12.5% equal shareholding to each of the directors Evan Jankelowitz, Mohammed Kalla and Kundayi Munzara. The acquisition aims to expand the firm's global reach and tap into RMI's distribution and operational capabilities. The change in shareholding means that the firm's BEE rating is subject to review, but prior to expiry in November 2016 the firm was rated BEE level 2 contributor.

Philosophy and process

The owner-managed firm believes that a singular focus on property, combined with a relatively small and nimble team, allows them to execute efficiently and effectively on investment ideas. While long term value investment remains the core tenet, the specialist approach means that the team can exploit short-term growth opportunities. In brief, the team has identified key pillars for their investment decisions:

- Thorough fundamental research
- Detailed financial analysis and modelling of risks and returns
- An understanding of the broader macroeconomic fundamentals which drive property values and trends
- Evaluation on a property by property basis
- An ability to take shorter run views on corporate actions and deals in the sector which can add value

They focus on an extended investment horizon in order to smooth out the short-term fluctuations associated with interest rate cycles, where ultimately the companies with a well-positioned portfolio and strong management teams, will prevail. To achieve this, they look to identify companies that display quality long term earnings prospects, have a portfolio of assets with the potential to generate above average growth in their rental streams and are trading at reasonable values relative to their growth prospects. Once the team has identified well-positioned companies, they consider a number of additional factors before inclusion: Liquidity constraints, quality and fit with the overall portfolio in terms of exposure to specific risks, cashflow profiles, revenues and costs associated with the properties and management thereof, company's potential to raise equity from the market, corporate actions or acquisitions that will impact earnings and prospects for distribution growth and developments in local and offshore bond markets which will impact relative yields.

The investable universe consists of property companies listed on the main board of the JSE. The team leverages off its experience in the sector and industry relationships, as well as constant communication between the close-knit team, to generate ideas. A proprietary in-house ranking table and the stock analyses performed by the investment managers (Evan, Kundayi and Mohamed) informs the agenda of the twice-weekly stock meetings. Decisions on the buy/sell/hold list are taken at these meetings and require a majority vote from the team. The quantitative aspects of the research consolidate the selected universe of stocks into a ranking table. Longer-dated models are used in order to define the long term strategic holdings, while tactical calls are dictated through a shorter-dated ranking table. Cognizance is also taken of risk through sector, strategy and to a lesser extent regional diversification and attention is paid to key aspects such as financial gearing and asset quality relative to where the sector may be in a particular cycle.

The firm makes use of proprietary in-house models to monitor the fund's positions relative to the index, its tracking error and the contributors to tracking error and beta. The rebalancing process is outlined below:

Portfolio construction is in line with the JSE index review calendar, but interim adjustments such as corporate actions would result in portfolio rebalancing.

Benchmarks are estimated a few days in advance, based on the index adjustment information disseminated by the JSE.

The trades which will be necessary to get the fund in line with the estimated benchmark are calculated in advance, so that they can be executed on the auction day. Prior calculation allows the team to avoid lumpy trades and plan for any liquidity/issuance constraints.

Team

The team has a solid background in the asset management industry. Evan Jankelowitz, in his capacity as Co-Head, helped to grow the Stanlib Listed Property Franchise business into the largest listed property manager in South Africa at the time and consistently achieved top decile performance. Mohamed Kalla started his career at RMB, and gained exposure to various aspects of fund management before moving on to a position as Research Analyst at Barnard Jacobs Mellet. While with BJM, he was one of the top-rated sell-side analysts in the Real Estate sector. Kundayi joined his two co-founders from Investec. His roles at Investec included being a buy side analyst, head of research for the investment team and co-manager for global bespoke private client Real Estate Investment Trust portfolios in London. Prior to joining Investec Property Investments, Kundayi was part of the valuation teams at Investec Private Bank and Old Mutual Properties. Non-core activities and responsibilities are outsourced to allow the investment managers to focus on investment management.

Product commentary

The team aim for a targeted total return to outperform the FTSE/JSE Listed Property index ("SAPY Index") over a 3 to 5 year investment horizon. The Fund has managed to deliver a consistent, low-risk outperformance of the benchmark, returning excess performance of 2.7% since inception (November 2011). The team has taken advantage of political uncertainty and depressed local economic conditions to consolidate their positions in established, listed companies, particularly those which have continued to grow their income distributions (e.g. Growthpoint). Brexit and global uncertainty have provided opportunities to upweight diversifying positions in selected companies with higher offshore-exposure (e.g. NEPI).

Fees and costs

The total investment cost for the unit trust comprises the Total Expense Ratio (service fee + performance fee + VAT) and any transaction costs. The Total Investment Charge (TIC) is 1.65% for class A1 – with 0.25% transaction cost, zero performance fees an annual service fee of typically 1.25% and VAT.

Stanlib Inflation Linked Bond Index Fund

ASISA Classification

South African - Interest Bearing - Variable Term

Firm

Stanlib was established in 2002, following a merger of the Liberty and Standard Bank Group's asset management, wealth management and unit trust businesses. The merger effectively cemented the collaboration between two well-established companies, both dating from the 1960s.

In June 2003, the Standard Bank and Liberty Life Groups sold 25.2% of Stanlib to a BEE consortium known as Quantum Leap Investments 740 (Pty) Ltd. At the end of 2006, Quantum Leap sold its stake in Stanlib to Liberty Life. It was also agreed that Liberty Life would purchase Standard Bank's stake in the business. This transaction resulted in Stanlib becoming 100% owned by Liberty Life.

In 2010, Stanlib formalised a franchise model to manage investments. The franchises are made up of focused teams of investment professionals, who are specialists in their disciplines and responsible for managing clients' assets in their areas of expertise. These franchises are Multi-Asset, Equity, Direct Property, Listed Property, Fixed Interest, Absolute Return, Africa, Alternatives and Stanlib Multi-Manager.

Stanlib's assets under management and administration as at 30 June 2016 were R584 billion, of which the Inflation Linked Tracker Fund makes up R64 million. Stanlib, a wholly owned subsidiary of Liberty, shares the parent company's status as a Level 2 BEE contributor.

Philosophy and process

The firm believes that it can implement a combination of low-cost passive investments and alpha generating active investments to generate superior long-term returns for clients. The firm's overall process consists of conducting three forms of analysis: the team would conduct a top-down, sector and individual company analysis when determining how they would construct a portfolio. The company analysis is generally considered after the team has gained a thorough understanding of the prevailing economic environment. This naturally leads to the top-down analysis being the starting point of their investment decision-making process. The top-down analysis would cover multiple macro variables such as interest rate cycles and economic growth. These variables are key indicators used within the team's investment decision-making framework. Given the importance of this process, the Stanlib investment team conduct a quarterly top-down and bottom up tactical asset allocation analysis. This quarterly meeting includes investment professionals across the various Stanlib franchise businesses. This allows the investment teams to identify and debate certain opportunities and risks within their respective areas. The two-day quarterly review covers economics, industry analysis and detailed analysis of the fixed income, listed property and general equity markets. By its nature, a tracker fund requires regular and fairly predictable decisions to be taken around certain events. The team will therefore discuss and agree in advance on the course of action in dealing with client cash flows, corporate events and rebalancing of the fund for changes in the underlying index. While the formal quarterly review is a useful additional platform for generating ideas on how to handle such events, the team works together in an open plan environment, facilitating exchange of ideas. Decisions are by consensus.
The premises underlying the management of the Tracker Fund are in line with the firm's overall philosophy regarding quantitative investments :

* Portfolio returns are ultimately determined by beta, not by alpha
* Quantitative analyses and models are useful tools in constructing beta solutions
* Beta can be managed in a structured and clinical way, thereby avoiding sentiment-driven losses
* Diversification within and across asset classes improves overall portfolio outcomes
* Quantitative processes can provide low cost solutions, therefore improving investment outcomes.

The firm makes use of proprietary in-house models to monitor the fund’s positions relative to the index, its tracking error and the contributors to tracking error and beta. The rebalancing process is outlined below:

Portfolio construction is in line with the JSE index review calendar, but interim adjustments such as corporate actions would result in portfolio rebalancing.

Benchmarks are estimated a few days in advance, based on the index adjustment information disseminated by the JSE.

The trades which will be necessary to get the fund in line with the estimated benchmark are calculated in advance, so that they can be executed on the auction day. Prior calculation allows the team to avoid lumpy trades and plan for any liquidity/issuance constraints.

Team

Portfolio manager Teboho Tsotetsi started his career at the South African Reserve Bank, where his role as risk analyst included validating the South African commercial banks’ risk models for Basel compliance. He joined Stanlib as quantitative analyst in 2007, specialising in asset allocation, risk management, portfolio construction and multi-factor risk modelling. Quantitative analyst AnnTaylor provides key support in these areas. Teboho is assisted in the implementation of his fixed interest view by Ran Basdeo, the manager of the ETF portfolios and a registered securities traded. His 9-year background with the firm has seen him exposed to the execution of trades in the Fixed Income team, in the Alternative Investments space and with the Offshore Trades Processing teams.

Product commentary

The Stanlib Inflation Linked Bond Index Tracker Fund is a passively manage product, which aims to replicate the performance of the SSA Inflation Linked Government Issued Bonds index (iGov index) as closely as possible. The ideal is to have a zero tracking error, but since the fund is required to hold some cash and since there are some liquidity constraints, a tracking error of just below 0.1% over the three year period can be expected.

The portfolio has managed to perform in line with the benchmark and has delivered a 2.59% annualised return since inception(net of fees to December 2016).

Fees and costs

The Total Expense Ratio (TER), showing the charges, levies and fees relating to the management of the portfolio, is 0.67%. The Total Investment Charges (TIC) consists of the TER and the Transactions Costs (expenses incurred relating to the buying and selling of underlying fund assets). The TIC for this fund is 0.67%, as it is indicated that zero transaction costs are passed through to unit trust investors.