

The fund generated a return of 9.4% for the first quarter of the calendar year, comfortably ahead of the return of the financial index of 7.3%. Over one year the fund has returned 26.3%, and over three years a compound annual return of 40.2%.

The quarter was once again a strong one for the banks, with the fund's three significant investments all gaining about 13%. After a volatile year for share prices, the 2006 financial results from the banks confirmed that the industry continues to grow strongly. Record levels of advances growth and improved margins boosted net interest income, while higher transaction volumes and strong equity markets supported non-interest revenues. Tighter monetary conditions have resulted in an increase in credit impairments, but these are well within expectations and still below what we would consider to be normalised levels. And while expenses growth was reasonably high, at least a portion of this can be attributed to investment in future growth. The past five years has marked a period of extremely rapid expansion in consumer credit, which has driven strong performances from retail banking operations. Encouragingly, the growth in consumption and the positive economic environment is now starting to translate into increased capacity utilisation, placing pressure on businesses to expand. As a result, growth in corporate advances has started to increase to levels similar to those of retail advances, a trend that is likely to continue. In future we expect the contributions from retail and corporate banking to be more evenly balanced than has been the case in the past.

The general financial sub-sector was also a strong performer for the quarter, and the holding in three of these stocks has contributed to the fund's out-performance. Brait, Coronation, and JSE are all businesses that benefit from higher equity market levels (albeit in slightly different ways). In times of sustained equity market strength, revenues tend to increase at a faster rate than costs, and good operational gearing is typically generated. While this appeared to have been largely ignored by the market in 2006, the shares have subsequently performed strongly.

Despite reporting good results (on the whole) for 2006 the life insurance sector delivered a poor return of 1% for the quarter. This is in no small part attributable to the arrival of a new regulatory headwind, this time in the form of governments proposed social security reform. A cornerstone of the proposals is the establishment of a national savings and risk scheme to which a minimum level of contribution by all employed people will be mandatory. The scheme is noble in intention, and is likely to go a long way to ensuring that low and middle income earners provide adequately for retirement.

However, the proposals are likely to result in funds being drawn away from the private sector, which for an equity investor in life insurance companies is not positive in the long run. This is an enormously complex overhaul of the retirement industry for which much of the detail still needs to be determined, and this will take some time. Government is working towards an implementation date of 2010, which to us seems unrealistically optimistic.

Given the scarcity of detail, it is difficult to quantify the impact of the proposals, or to determine which of the life insurers will be impacted most and which least by these reforms. In the shorter term there is unlikely to be a significant impact on the industry. It is the medium to longer term impact that concerns us, and as a result we have taken the decision to reduce the fund's holding in Liberty Group. Our investment in this business has for some time made up a large holding of the fund, and this was not a decision lightly taken. The move was motivated by the fact that, relative to the other life insurers, a greater portion of our assessment of the value of the company derives from the business's value of in-force (the present value of profit on business already written but to be recognised in future) and the value of new business yet to be written. It is these two components of the valuation that will be impacted by the reforms and which will remain under pressure for some time to come. While at the current share price, the investment opportunity would still seem reasonably compelling, the level of uncertainty and therefore risk has increased. It is for this reason that we can no longer justify the size of the position previously held.

We remain optimistic on the outlook for the financial sector as a whole. Banks have re-rated somewhat to a level where they trade on forward PE's of 11 to 11.5 and dividend yields of 3.5%-4%. Given our medium term earnings growth expectations for the sector, these valuations do not look excessive. Domestic insurers appear inexpensively priced and continue to trade at discounts to their embedded values, with the prospect of ongoing improvements to capital efficiency. However, until there is more clarity surrounding the social security reforms, regulatory uncertainty is likely to hang over the sector.

**Neill Young**  
Portfolio Manager

Fund category	Domestic Equity Financial
Launch date	1 July 1998
Portfolio manager	Neill Young
Fund size	R1 billion
NAV	2840.23 cents
Annual management fee	1.43% (incl VAT)

Benchmark	FTSE/JSE Africa Financial Index
Fund description	Invests in a broad range of financial shares, including banks, insurance and investment companies.

### EFFECTIVE ASSET ALLOCATION EXPOSURE

Sector	31 Mar 2007
<b>Domestic Assets</b>	<b>100.00%</b>
<b>Equity</b>	<b>97.69%</b>
Financials	97.69%
<b>Real Estate</b>	<b>0.15%</b>
<b>Cash</b>	<b>2.16%</b>
<b>International Assets</b>	<b>0.00%</b>

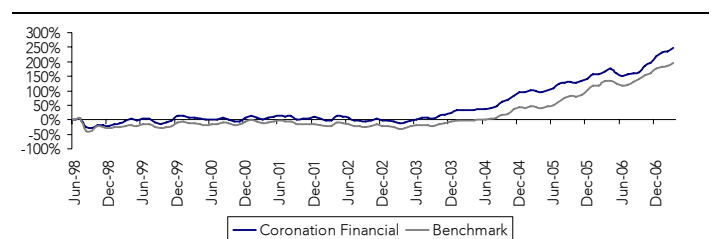
### PERFORMANCE AND RISK STATISTICS

	Fund	Benchmark
Year to date	9.40%	7.27%
Latest 12 months	26.26%	27.25%
Latest 36 months (annualised)	40.15%	41.18%
Latest 60 months (annualised)	30.45%	29.02%
Since inception (annualised)	15.86%	12.38%
Annual deviation since inception	21.61%	24.29%
Sharpe ratio	0.22	0.05
Maximum gain	53.63%	80.40%
Maximum drawdown	-30.89%	-39.78%
Positive months	62.86%	63.81%

### TOP 10 HOLDINGS

As at 31 March 2007	% of Fund
Standard Bank Group Ltd	20.79%
FirstRand Ltd	18.40%
Absa Group Ltd	11.29%
Liberty Group Ltd	11.06%
Discovery Holdings Ltd	10.44%
Metropolitan Holdings Ltd	8.18%
Brait S.A.	3.90%
Remgro Ltd	3.22%
Coronation Fund Managers Ltd	2.95%
Nedbank Group Ltd	2.86%
<b>Total</b>	<b>93.09%</b>

### CUMULATIVE PERFORMANCE SINCE INCEPTION



### INCOME DISTRIBUTIONS

Declaration	Payment	Amount	Dividend	Interest
31/03/2007	01/04/2007	48.55	47.47	1.08
30/09/2006	01/10/2006	46.90	45.39	1.51
31/03/2006	01/04/2006	13.80	12.45	1.35
30/09/2005	01/10/2005	34.72	32.20	2.52

### ANNUAL RETURNS SINCE INCEPTION

	Fund	Benchmark	Active Return
2006	28.83%	35.83%	-7.00%
2005	32.02%	34.69%	-2.67%
2004	57.09%	52.38%	4.71%
2003	25.19%	17.92%	7.28%
2002	-9.27%	-8.24%	-1.03%
2001	2.90%	-9.53%	12.43%
2000	-5.55%	2.93%	-8.48%
1999	42.51%	29.83%	12.68%
1998	-21.13%	-29.04%	7.91%

### MONTHLY PERFORMANCE RETURNS

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Fund 2007	4.43%	0.27%	4.47%									
B'mark 2007	2.85%	1.10%	3.16%									
Fund 2006	7.01%	0.60%	3.69%	0.43%	-5.96%	-4.35%	2.94%	1.45%	1.68%	7.56%	3.63%	7.94%
B'mark 2006	7.74%	0.08%	6.19%	1.13%	-4.96%	-2.22%	1.14%	4.43%	4.08%	6.02%	2.33%	5.85%