

## Class A

as at 31 March 2007

Fund category	Domestic Fixed Interest Varied Specialist
Fund launch date	2 October 2006
Portfolio managers	Tania Miglietta and Godwill Chahwahwa
Fund size	R141.8 million
NAV	95.51 cents
Annual management fee	0.68% (incl VAT)
Initial fee	0.00%

Benchmark	Alexander Forbes 3-month (STeFI) Index, tax adjusted for maximum individual tax rate
Fund description	Invests in a range of quality listed preference shares with the aim of maximising yield in the form of dividend income.

## ASSET ALLOCATION

Sector	31 Mar 2007
<b>Domestic Assets</b>	<b>100.0%</b>
Bank issued preference shares	53.2%
Corporate issued preference shares	35.5%
Ordinary equity	2.1%
Cash	9.2%

## PERFORMANCE RETURNS

	Fund	Benchmark
Since inception (unannualised)	N/A	N/A
Annual deviation since inception	N/A	N/A
Sharpe ratio	N/A	N/A
Maximum gain	N/A	N/A
Maximum drawdown	N/A	N/A
Positive months	N/A	N/A

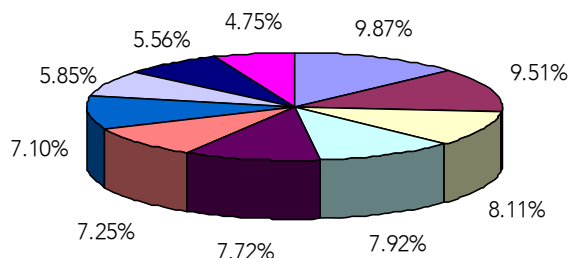
Performance figures will be published once a six-month track record has been established.

## INCOME DISTRIBUTIONS

Declaration	Payment	Amount	Dividend	Interest
31/03/2007	01/04/2007	2.04	1.96	0.08
31/12/2006	01/01/2007	1.23	0.89	0.34

## TOP 10 HOLDINGS

As at 31 March 2007



## TOP 10 HOLDINGS: YIELD AND CREDIT RATING

Preference Share	Annual yield	Credit rating
Absa Bank Ltd	9.4%	AAA
Standard Bank Group	9.6%	AA+
FirstRand Bank Ltd B	9.4%	AA+
Nedbank Ltd	9.6%	AA-
Imperial Ltd	9.8%	A+
Investec Non Red Cum Ltd	9.6%	A+
Investec Ltd	9.3%	A+
Network Healthcare Ltd	9.9%	A
PSG Ltd	10.5%	A-
Grindrod Ltd	10.8%	BBB+

- Investec Ltd Preference Share
- Investec Ltd Non Red Cum Preference Share
- Network Healthcare Ltd Preference Share
- Nedbank Ltd Preference Share
- Grindrod Ltd Preference Share
- Imperial Ltd Preference Share
- Standard Bank Group Preference Share
- PSG Ltd Preference Share
- FirstRand Bank Ltd B1 Preference Share
- FirstRand Bank Ltd B Preference Share

## PORTFOLIO MANAGER COMMENTS

"Weathering the perfect storm"

The preference share market experienced what can be termed the perfect storm in the past quarter. A number of events generated uncertainty among investors in preference shares, which led to significant price weakness. The preference index that we have compiled<sup>1</sup> to represent our investable preference share universe returned -4.86% while the fund gave -3.77% total returns for the quarter.

The first source of uncertainty came about during the finance minister's budget speech on the 21st of February 2007, when it was announced that Standard Tax on Companies (STC) would be phased out and replaced by dividend tax in two stages, as follows:

- Stage 1 runs from 1 October 2007 to 2008 and it involves the lowering of the STC rate from 12.5% to 10%.
- Stage 2 runs from 2008 onwards, where the STC will be replaced by a dividend tax, in the hands of the investor.

The attraction of preference shares for the individual investor is the *after-tax yield* earned. In the absence of any compensation to preference share investors, these changes would have meant that the after-tax yield would fall by the amount of dividend tax levied, in this case 10%. This precipitated uncertainty and panic selling of preference shares.

This sell off did not take into account the spirit encapsulated in the "change in tax status" clause included in most preference share listing documents. This clause was interpreted to mean that the issuer of the preference share would take steps to pass on the benefit of the STC saving to investors, thereby neutralising the effect of the legislative changes.

We have subsequently seen most of the issuers of preference shares publishing announcements, reassuring the market of their intention to ensure that these changes are not negative to preference share holders. While this has served to bring more certainty and confidence to the market, prices have not recovered. In the fund, we took advantage of the price weakness to add to our preferred stock picks where volumes allowed.

During the month of March, we had two preference share announcements for the further issuance of Absa (ABSP) and Nedbank (NBKP) preference shares. The new Absa (ABSP) issue came to market at 75% of prime when the original issue had been priced at 63% of prime. ABSP carries the highest credit rating at AAA and therefore had the effect of pushing all other lower rated preference share prices down, equivalent to a de-rating for the sector. We have therefore seen further price weakness across the preference share market as a result of this.

Currently our fund yields 9.3% (after tax and before fees) and we believe that this represents a very attractive opportunity to invest into what is a very cheap market in our view. The fundamentals of preference shares remain intact and in fact, most preference shares are still pricing in a lot of uncertainty and negativity around the proposed STC changes. In the fund, we have taken the opportunity to add to positions where we see under-valuations. The new issues coming to the market have also allowed us to benefit from arbitraging out opportunities where the new tap issue is priced lower than the existing issue. We have also pursued other investments away from preference shares, where the after-tax returns earned exceeded that of the preference share universe without unduly increasing the risk of the fund. This was done within the 30% limit that allows for alternative investments in the fund.

Have we fully weathered the perfect storm yet? Timing the bottom is always a difficult call and therefore we will not attempt to call the bottom. Certainly a lot of the potential risks to preference shares have played themselves out. We believe that in this case, where others see adversity, we see opportunity.

<sup>1</sup> *Comprising all preference shares with nominal market value in excess of R10m.*