

PORTFOLIO MANAGER COMMENTARY

Whereas the calendar year started slowly for equity markets around the world, the month of March brought lots of joy. This resulted in respectable returns being produced by these markets over the first three months of 2010. The South African equity market was up 4.5% over the period, with bonds rerating strongly to produce 4.4%. Listed property returned 9.9% and preference shares 7.8%, while inflation-linked bonds showed virtually 0% return over the period. The rand strengthened by 1.5% over the quarter against the US dollar, and by a whopping 6.7% against the euro. The MSCI World Index returned 3.4% since the start of the year, with developed equity markets actually outperforming emerging markets for the first time since the rebound started. Within developed markets Japan and the United States outperformed Europe by some margin.

Against this backdrop the fund had a strong quarter. The three-month return of 3.5% exceeded the benchmark of inflation plus 4%, but more importantly, the 12-month return of 21.4% and the 5-year number of 14.2% per annum compare favourably with both the benchmark and some of our peers in the sector. Since inception the fund has returned 15.4% per annum versus the benchmark's 10.6% per annum.

Once again our equity holdings contributed strongly. Stock selection was good, with the equity portion of the fund outperforming underlying indices by a wide margin. The most significant contributors amongst the equity holdings were Standard Bank, Woolworths, Tiger Brands, Mondi, AVI, and Remgro. A gratifying aspect of the attribution analysis is the fact that very few of our equities detracted from performance in absolute terms. MTN (our biggest holding where we continue to hold a very positive view on the stock), Pan African Resources, AngloGold, and Hulamin were the only real detractors.

Domestic property contributed positively and we have used the strength in this sector to reduce the fund's exposure further. The fund's preference shares benefited from a strong rerating in that sector. The big position in inflation-linked bonds has not yielded positive results yet, but we continue to hold the view that it is an attractively priced asset over the medium term. We are accumulating more of these instruments at acceptable prices.

Our international exposure performed well in dollar terms. Unfortunately the strength of the rand pared these gains. During the period we continued to consolidate our international exposure into a few pooled vehicles managed actively by ourselves. This has already led to increased focus and a greater alignment of investment objectives. We continue to advocate a full offshore position, and will manage the fund to achieve this goal. We think that the rand is vulnerable to changes in risk appetite, and on top of this view (that at the best of times cannot be classified as a high conviction view) we continue to prefer offshore equities to domestic equities.

Investors around the world are embracing risk again. Whereas the economic outlook for many of the troubled economies has improved over the last few months, one has to be wary in terms of how much of this good news has already been priced into financial markets. We have already bought quite a number of put options against the equity holdings in the fund. We have also introduced written call options on some of our equity holdings where we think the upside has reduced as a result of price action. We will continue to be true to the absolute return objectives of the fund in our future dealings.

Portfolio managers

Louis Stassen and Henk Groenewald