overberg asset management

Local performance factsheet

OAM Local Real Return Portfolios

ZAR Rand

NOV 2012

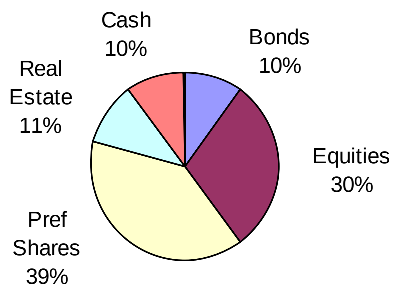
Technical Details

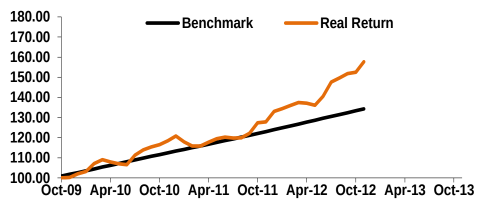
- **FSB** approved
- Base currency: **South African Rands**
- Minimum investment: **R500 000**
- Benchmark: **Prime Interest Rate**
- Asset Allocation: **flexible mix of bonds, listed commercial properties, pref shares and ordinary shares.**

Investment Objectives:

- conservative growth with income
- consistent annual real returns
- low volatility

ASSET ALLOCATION





(As calculated by Overberg 30 Nov 2012)

	Real Return %	Benchmark %
Annualised Total Return	15.91	10.03
2010	17.58	11.42
2011	10.14	9.38
YTD	18.49	8.34

*Since March 2005: All performance figures include income and are net of fees and expenses

Growth 2012	Real Return %	Benchmark %
January	0.98	0.75
February	1.17	0.75
March	1.10	0.75
April	-0.22	0.75
May	-0.76	0.75
June	3.29	0.75
July	5.00	0.71
August	1.43	0.71
September	1.43	0.71
October	0.41	0.71
November	3.41	0.71

	%
Annualised Income Yield	10.35

Introduction

Overberg Asset Management specialises in the management of individual portfolios, tailored to the investment objectives of each client. As an independent company, Overberg can set objective standards in its selection of investments. Privately managed portfolios provide clients with the optimal investment solution. Lower cost structures, greater maneuverability and meaningful exposure to smaller companies or tomorrow's "blue chips", all help to generate superior investment returns. Moreover, privately managed portfolios can be tailored specifically to individual requirements. At the cutting edge of investing, Overberg has a proven track record in global and domestic South African markets. Your portfolio will be in the safe custody of BOE Securities, Investec Securities or Standard Equities.

Overberg's Real Return Portfolio is an enhanced alternative to either money market funds or bank deposits, offering the prospect of better after tax returns by generating a sizeable portion of income from dividends. Yield is increased by active management across SA government and parastatal bonds, pref shares and growth assets including listed commercial property and high yielding ordinary shares. Valuation volatility is kept at a minimal level with temporary valuation declines not expected to exceed 5% of the value of the portfolio at any point in time. This is achieved through disciplined asset allocation ranges, and diversification across asset classes and individual holdings. A small, actively managed exposure to growth assets will enhance after tax yields with a minimal increase in risk.

Commentary

The economic outlook has deteriorated significantly in the wake of the industrial unrest over the past three months. At the same time the inflation outlook has worsened due to elevated global food and fuel prices and the weakening rand. The rand has depreciated sharply in response to the widening current account deficit and the souring of foreign investor sentiment following the Marikana tragedy and the downgrading of SA's sovereign debt ratings.

After Moody's downgraded SA's credit rating, brining it in line with other rating agencies, Standard & Poor's (S&P) followed with a further downgrade in October, taking its rating down from BBB+ to BBB, citing rising public wage expectations, service delivery issues and uncertainty regarding government policy leading into the ANC's leadership conference in Mangaung in December. SA is now only 2 notches above non-investment grade according to Moody's and Fitch and only 1 notch above according to S&P. A relegation to non-investment grade would result in exclusion from the Citigroup World Government Bond Index (CWGBI) into which SA has only recently been included, and so could prompt a reversal of recent bond inflows. The rating agencies have kept SA on "negative outlook" implying a further downgrade is likely unless conditions improve.

Most macro-economic data signal an increasingly unbalanced economy with spending continuing to outpace production. As a result imports remain elevated while exports are falling, causing an unsustainably high current account deficit. A spike in iron ore output helped limit damage to mining output in August, which managed year-on-year growth of 0.8% albeit down from 7.1% in July. However output is likely to have deteriorated further since then with strikes spreading from platinum to the gold sector. Growth in manufacturing output also weakened in August to just 3% on the year and the weaker trend is set to continue according to the forward looking Kagiso/ BER index which deteriorated sharply to 46.2 in September. The index recovered slightly to 47.1 in October but remains well below the critical 50 level which signals contraction as opposed to expansion.

The country's balance of payments deteriorated markedly over the 3rd quarter with exports declining 2% on the year and imports rising 12.6%. The trade deficit widened dramatically to R13.8 billion in September taking the cumulative deficit for the year to date to R86.1 billion from only R5.1 billion over the equivalent period in 2011. The current account deficit is forecast to widen from 3.3% of GDP in 2011 to around 6% in 2012. Consumer spending remains strong with retail spending increasing a much higher than expected 6% year-on-year in August, suggesting the rising demand for imported goods will continue unabated.

The rand remains vulnerable in spite of its relative stability in October. Industrial unrest, the widening current account deficit, sovereign credit rating downgrades and continued uncertainty in the run-up to the ANC elective conference in December are likely to keep the currency under pressure, precipitating a potentially sharp sell-off if perceptions deteriorate further. The foreign appetite for SA bonds appears to be moderating with monthly inflows decreasing from R19.3 billion in June, R15.2 billion in July to just R4.7 billion in August, recovering only slightly to R8.3 billion in September and R8.7 billion in October in spite of SA's inclusion in the CWGBI on the 1st October. Meanwhile foreigners have been disinvesting from equities by R10.6 billion for the year to date. The SA Reserve Bank also predicts further rand depreciation according to its real equilibrium exchange rate, which calculated using real interest rate differentials, productivity measures, commodity prices, the fiscal balance and capitals flows, confirms the rand is overvalued by around 3%.

The Minister of Finance Pravin Gordhan delivered a solid Medium Term Budget Policy Statement. While reporting a slight increase in budget deficits over the next three years compared with forecasts made in the annual Budget earlier in the year, this is due solely to a decline in economic output as opposed to increases in government expenditure. The Treasury remained committed to prudent and conservative fiscal policy. In October the SA Reserve Bank also released its bi-annual Monetary Policy Review which highlighted rising inflationary pressure from global fuel and food prices. Nonetheless consumer price inflation is expected to remain below the 6% target level and drift lower from next year onwards, averaging 5.2% in 2013 and 5.0% in 2014. Under normal circumstances a benign inflationary outlook would pave the way for further monetary easing in the context of slowing economic growth but scope for additional rate cuts is being undermined by the vulnerable rand and the impact a weaker rand could have on inflation. Furthermore, an interest rate cut would provide little benefit to the production side of the economy, which is in most need of help. An additional rate cut may just serve to exacerbate the current account deficit by further stimulating consumer demand and demand for imports.

Despite the bleak economic outlook the JSE All Share Index (ALSI) has continued to rise to successive all-time record highs. The average price to earnings multiple of the ALSI is currently 12.90 which remains below the long-term average of 14.01 suggesting valuations are slightly below historic fair value. While recognizing the value remaining in equities especially compared with other asset classes, our current portfolio strategy is increasingly geared towards rand hedge stocks due to the likelihood of further rand depreciation. At the same time as domestic risks are rising conditions in developed economies are brightening. The improving outlook for developed economies and their currencies should dampen the trend of the last few years towards emerging market currencies. We believe that the best opportunities lie in rand hedge stocks and plan to increase the overall rand hedge exposure of the portfolios as we go into 2013.