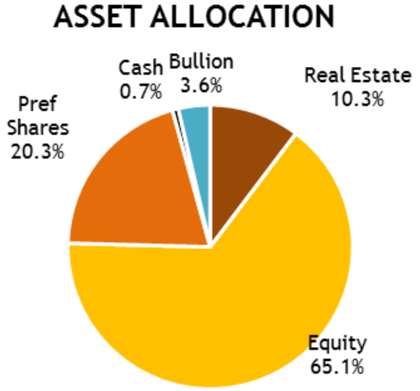
OAM Local Growth Portfolio[1]

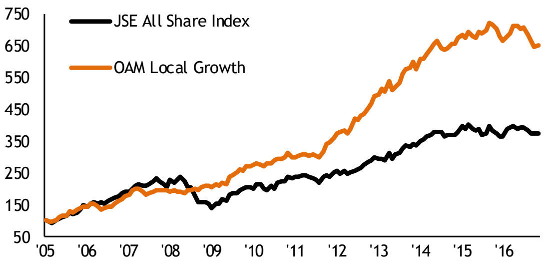
Technical Details

- Base currency: **South African Rands**
- Benchmark: **JSE All Share**
- Asset Allocation: **Flexible mix of equities, bonds and cash**

Investment Objective

- conservative growth
- consistent annual returns
- low volatility





(As calculated by Overberg Jan 2017)

1) Individual portfolio representing Local Growth investment style

December 2016

	Growth %	Benchmark %
Annualised Total Return	17.15	10.87
2005	39.51	34.28
2006	21.14	28.47
2007	14.39	16.23
2008	7.13	-25.27
2009	28.32	28.63
2010	15.05	16.09
2011	10.52	-0.41
2012	35.70	22.71
2013	28.25	17.85
2014	9.71	7.60
2015	7.07	1.84
2016	-7.69	-0.06

Return over 3, 5 and 7yrs	2.73	13.54	13.32

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

Growth 2016	Growth %	Benchmark %
January	-3.85	-3.05
February	-1.58	0.58
March	2.11	5.71
April	1.06	1.35
May	3.86	1.79
June	-0.53	-3.13
July	-1.17	1.11
August	0.52	-0.12
September	-3.21	-1.49
October	-2.43*	-2.62
November	-2.76*	-0.75
December	0.32	0.88

	%
Annualised Income Yield	1.83

* - Restated

Market Review

With the exception of financial stocks all South African equity indices suffered losses during the fourth quarter (Q4). The Financial 15 index eked a small gain of +2.4% although for 2016 as a whole lost -1.0%. Conversely the Resources 10 index lost -1.1% over the quarter but was the only sector to post gains for the year with a solid +26.4% return. Although impressive, the Resources index still hasn't reversed the -39.4% loss in 2015. The Industrial 25 index fared worst due to the impact of rand strength on the large dual listed stocks, with respective losses for the quarter and year of -5.8% and -10.4%. As a result, the All Share index offered little respite losing over the quarter and the year by -2.5% and -0.1% similar to 2015's slender gain of +1.8%. Despite the dollar's resurgence, the rand rallied against the US currency by an additional +1.1% in the final quarter culminating in a +10.3% appreciation over the year from R/$15.28 to R/$13.70. The dollar gold price maintained an +8.5% gain in 2016 from $1060.9 to $1150.9 although well off its peak levels following a -12.5% loss in Q4.

GDP grew in the third quarter (Q3) by just 0.2% quarter-on-quarter annualised in stark contrast to the upwardly revised 3.5% growth in Q2 and below the 0.6% consensus forecast. Manufacturing production, which supported GDP growth in Q2, contracted in Q3 by -3.2% annualised. Agricultural output shrank for a seventh straight quarter although to a lesser degree, by -0.3% compared with -0.8% in Q2. On the plus-side, mining production grew by 5.1%. Without the contribution from mining, overall GDP would have contracted by -0.1%. GDP is expected to fare only slightly better in Q4 resulting in overall GDP growth in 2016 of 0.4%. However, GDP growth is expected to lift to 1.2% in 2017, with stronger contributions from manufacturing, mining and agriculture. Consumer spending should also recover in line with easing inflation and a gradual decline in interest rates in the second half of the year. Expectations for stronger growth should also boost fixed investment spending.

The Barclays manufacturing purchasing managers' index (PMI) increased from 45.9 in October to 48.3 in November. Although in sub-50 contraction territory for a fourth straight month some of the sub-indices showed decent gains. Manufacturers' purchasing commitments increased from 46.7 to 50.0 and the forward-looking new sales orders and expected business conditions regained the key 50-level, rising from 44.5 to 51.4 and from 50.6 to 53.9. The data suggests the manufacturing sector will trough in Q4 and improve into the first half of 2017 recovering off this year's low base. Domestic manufacturing demand will be helped by a recovery in fixed investment and the boost to consumer spending from lower inflation and interest rates. Export-oriented manufacturing should benefit from rising global commodity prices and a US-led increase in global economic growth.

Mining production will be aided by the improving outlook for global commodity prices amid growing infrastructure spending in China and the US. Firmer global commodity prices should maintain the recent stabilization in mining output although the long-term health of the industry will depend on greater regulatory certainty. Agricultural output will respond to the improved outlook for maize harvests this year. The maize crop fell from 9.95 million tons in 2015 to 7.5 million in 2016 but should exceed 10.5 million tons in 2017. The US Department of Agriculture reported earlier this year that South Africa's maize harvest could exceed 13 million tons due to favourable La Nina weather patterns.

Although still in negative territory the BER consumer confidence index increased from -9 in Q2 to -3 in Q3. Of the three sub-categories, consumers' expectation of economic performance in 12 months' time and expectation of households' financial prospects in 12 months' time, both recorded gains. The appropriateness of the present time to make durable goods purchases recorded a decline. Among income groups, the BER confidence index fell from -6 to -10 for high income households but increased sharply from -15 to +6 for those earning less than R7000 per month.

The South African Reserve Bank (SARB) December Quarterly Bulletin reported a widening in the current account deficit from -2.9% of GDP in Q2 to -4.1% in Q3. The deterioration is due to the trade account moving from a surplus of R47.9 billion in Q2 to a deficit of -R3.8 billion in Q3. On the financing side the current account deficit was counterbalanced by continued inflows into the capital account. Net portfolio inflows fell over the quarter from R30.9 billion to R22.4 billion, while net direct investment inflows increased from R2.1 billion to R5.6 billion. Although slightly disappointing the current account deficit is likely to resume its downward trend in the quarters ahead in response to improving global demand and the firming in commodity prices.

According to the SARB Quarterly Bulletin gross fixed capital formation fell in Q3 for a fourth straight quarter but the pace of contraction slowed from -6.8% quarter-on-quarter annualised in Q2 to -1.0% in Q3. Contraction in private sector capital spending reduced from -4.1% to -1.6% while government sector spending grew by 1.5% up from -11.2% in Q2. Meanwhile, employee compensation increased with annualised real household disposable income growth rising from 1.7% in Q2 to 2.0% in Q3. Household debt to disposable income fell from 75.1% to 74%, down from a peak of 80% in 2013, and the debt service ratio reduced from 9.7% to 9.6%. Fixed investment spending is expected to recover over the next year on expectations of an improving global and local economic outlook, while household finances and expenditure should benefit from declining inflation and a gradual reduction in interest rate.

The unemployment rate increased from 26.6% in the second quarter (Q2) to a record high 27.1% in Q3 despite a rise in the number of employed. A total 288,000 jobs were created during the quarter but the work force increased by 527,000. More encouragingly, the expanded definition of unemployment, which includes discouraged job seekers, edged lower from 36.4% to 36.3%. The highest number of jobs were created in the construction, finance, trade, agriculture and transport sectors, at 104,000, 103,000, 61,000, 56,000 and 53,000, respectively.

In its November policy meeting the SARB decided unanimously to keep its benchmark repo interest rate unchanged at 7.0%. Governor Lesetja Kganyago hinted that the interest rate hiking cycle is close to the end. The SARB forecast consumer price inflation (CPI) to peak in the final quarter at 6.6% slightly below its previous forecast of 6.7%, and maintains that CPI will fall back within its 3-6% target range in Q2 2017, which may prompt a reduction in interest rates in the second half of the year.

Finance Minister Pravin Gordhan gave a statesmanlike performance presenting the Medium Term Budget Policy Statement (MTBPS). Even though key fiscal measures deteriorated the overall reaction to the budget was positive. The budget deficit in financial year (FY) 2017 is expected to be 3.4% of GDP rather than the 3.2% projected during the State Budget. The FY 2018 budget deficit projection was raised from a previous 2.8% to 3.1%. Meanwhile, the debt-to-GDP ratio is projected to peak at 53.0% of GDP in FY 2019 compared with a previous projected peak of 51.0% in FY 2018. The Treasury reduced its GDP forecasts for 2016, 2017 and 2018 to 0.5%, 1.3% and 2.3%, respectively.

The MTBPS contained some disappointments. There was no mention of any major structural reform, which the credit rating agencies have highlighted as key to placing South Africa on a higher growth path. Despite a strikingly negative assessment Standard & Poor's (S&P) Global Ratings resisted downgrading South Africa's foreign currency sovereign bonds to "junk status". However, S&P like fellow rating agencies Fitch and Moody's kept the country on "negative watch" keeping open the threat of junk status in the next rating reviews in June and December. S&P and Fitch are one notch above non-investment grade and Moody's is two notches. The rating agencies cited political tensions and persistently weak GDP growth as key concerns.

In the three years to end 2016 the JSE All Share index gained by just +12%, an annual return of little over 3% and well below the return available in money markets. Although disappointing, we feel the outlook for equity returns has greatly improved from the current low base. There has never been a period longer than five years in South Africa in which equities have not outperformed money markets. There is evidence that the economy is bottoming out with signs of stronger economic growth, falling inflation and lower interest rates, which should boost consumer and business confidence. The equity market, being forward looking, will increasingly discount better times ahead. From the current trough company earnings are expected to grow by an aggregate 28.1% over the next twelve months, resulting in an attractive estimated forward price-earnings (PE) multiple of 15.8x. We are confident of a re-rating in equities in 2016 and are raising the equity weighting in portfolios to reflect this more optimistic outlook.