overberg asset management

LOCAL PERFORMANCE FACTSHEET

OAM Local Real Return Portfolios

ZAR Rand

APR 2015

Technical Details

- **FSB** approved
- Base currency: **South African Rands**
- Minimum investment: **R750 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

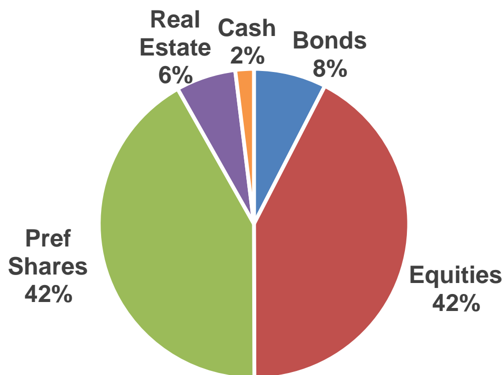
	Real Return %	Benchmark %
Annualised Total Return	12.42	9.68
2010	17.58	11.42
2011	10.14	9.38
2012	19.21	9.11
2013	11.86	8.84
2014	0.26	9.52
2015 YTD	7.02	3.12

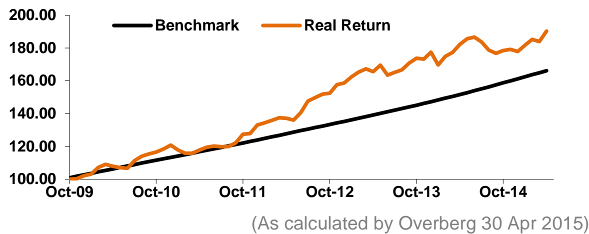
*Since March 2005: All performance figures include income and are net of fees and expenses

Growth 2015	Real Return %	Benchmark %
January	2.16	0.77
February	1.96	0.77
March	-0.68	0.77
April	3.45	0.77
May		
June		
July		
August		
September		
October		
November		
December		

	%
Annualised Income Yield	7.90

ASSET ALLOCATION





(As calculated by Overberg 30 Apr 2015)

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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 manoeuvrability 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 Nedbank Private Wealth, 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.

Quarterly Commentary 30 April 2015

The local equity market gained ground in the first quarter (Q1), driven mainly by rand hedge stocks, which benefited from the weaker currency. The market was also helped by strong global liquidity, especially in March when the Eurozone expanded its QE programme. While the Resources 10 index fell in Q1 by -2.19% in line with weaker commodity prices, other equity sectors performed strongly. The Industrial 25 and Financial 15 indices increased by 5.26% and 9.84% compensating for losses in resource stocks so that the All Share index finished the quarter with a gain of 4.85%. Although the rand depreciated by -4.16% against the US dollar the currency gained 0.53% versus the pound and 7.01% versus the euro. The All Bond Total return Index (1-3 year) returned a respectable 1.53% over the quarter. The gold price remained resilient especially in the context of a strengthening dollar, gaining 1.44% from $1183 to $1200.

SA's GDP growth rate accelerated sharply from 2.1% annualised in Q3 2014 to 4.1% in Q4. However, the rebound is attributed to a normalisation of activity in the manufacturing and mining sectors after the NUMSA strike in July and the lagged effects of the platinum strike. The manufacturing and mining sectors grew in Q4 by 9.5% and 15.2% annualised together contributing 2.3 percentage points to Q4 GDP growth. Most of the GDP rebound in Q4 is due to the low-base effect in manufacturing and mining and so is unlikely to be repeated in Q1 2015 especially in the context of intensified electricity shortages.

GDP growth is only expected to recover slightly from 1.5% in 2014 to around 2-2.5% in 2015. Although growth will be supported in the early part of 2015 by the drop in the petrol price the economy is facing numerous headwinds. The lack of reliable power supply, poor labour relations, limited and expensive transport and other economic infrastructure, rising production costs and increasingly interventionist and unpredictable economic policies will weigh on business and consumer confidence putting a ceiling on growth in 2015. On the expenditure side, household consumption expenditure will be limited from the second quarter onwards. The boost to disposable income from lower petrol and diesel prices will be reduced by higher taxes, the prospect of sharp hikes in electricity tariffs, and higher food prices given the drought in parts of the country. Consumer confidence will be constrained by weak employment growth, elevated consumer debt levels and strict lending criteria by financial institutions.

Gross fixed capital formation (GFCF) fell by -0.4% in 2014 as a whole, the first contraction since 2010. Private sector spending fell -3.4% due to subdued economic growth, regulatory uncertainty, energy and infrastructure

constraints. Unfortunately the outlook for investment remains poor. The latest RMB/BER business confidence index decreased by two points to 49 in Q1 below the key 50 level which demarcates expansion from contraction and does not bode well for private sector GFCF. Some sectors of the economy were especially impacted by electricity supply disruptions, pushing the manufacturing confidence index lower from 42 to 30 and the building confidence index from 66 to 49. The data indicates GDP growth being driven by an already heavily indebted consumer sector rather than the producing side of the economy.

Although delivering a fiscally prudent Budget Finance Minister Nhlanhla Nene's 2015/16 Budget did not keep to all the promises made in October in his Medium term Budget Policy Statement (MTBPS). Revenue projections were slightly lower and expenditures slightly higher causing the Budget deficit target to be revised upwards from -3.6% of GDP to -3.9%. In addition, there is further upside risk to expenditure from public sector wage negotiations which are underway to replace the current deal which expired at the end of March. Credit rating agencies will be particularly interested in the outcome of the ongoing public sector wage negotiations. Growing liabilities from state-owned enterprises (SOEs) add further risk to Budget expenditure projections. The biggest disappointment in the Budget was a lack of detail on which non-strategic SOEs would be sold to finance the bailout of Eskom and SAA. There had been assurances that a list of potential asset sales would be made available.

There is some good news. The SA Reserve Bank (SARB) Quarterly Bulletin shows the current account deficit narrowed more than expected from 6.0% of GDP in Q3 2014 to 5.1% in Q4 well below the 5.8% consensus forecast. The benefit to the trade balance of a sharply weaker oil price has not yet fully emerged given that imports of oil normally come through at forward rather than spot prices. Furthermore export growth is picking-up, especially in the vehicle sector. The National Association of Automobile Manufacturers forecasts a 10% increase in unit vehicle exports this year. The current account deficit is forecast to narrow further to 4.5% this year, helped by the fall in the oil bill, which together with petrol makes up around 24% of total imports.

Headline consumer price inflation (CPI) decelerated from 4.4% in January to 3.9% in February. However, February is likely to mark the trough in inflation. Inflation is set to move higher over coming months as a result of the large 9.5% month-on-month petrol price hike implemented in March and the 14% hike in April as a result of the fuel levy. Food prices are also likely to move higher as a result of the poor maize crop. Core CPI, which excludes food and energy prices, is already picking-up, up 0.7% on the month in February the highest increase in a year. CPI could potentially breach the upper end of the SARB's 3-6% target range by the end of the year, depending on the trajectory of the rand.

As expected the Reserve Bank's Monetary Policy Committee (MPC) unanimously decided to keep the repo rate unchanged at 5.75% in March. However, the statement was mildly hawkish, highlighting that the risks to the inflation outlook are to the upside. SARB governor Lesetja Kganyago reported that the outlook remains highly uncertain as a result of a lack of clarity on future oil prices and global monetary policy developments. Kganyago stressed that 'the MPC will remain vigilant and will not hesitate to act in order to maintain the integrity of the inflation targeting framework'. The SARB's short-term inflation forecasts were revised slightly upwards. CPI is projected to average 4.8% (previously 3.8%) in 2015 and 5.9% (previously 5.4%) in 2016. The SARB's GDP growth forecast for 2015 remained unchanged at 2.2%, while that for 2016 was revised from 2.2% to 2.3%. To balance inflation and growth the SARB is likely to keep rates steady for most of 2015, with a shallow rate hiking cycle towards the end of the year.

Private sector credit extension growth moderated from 9.2% year-on-year in January to 8.7% in February with growth in credit extended to households slowing from 3.5% to 3.3%. Corporate credit growth remained fairly strong at 13.6% which seems at odds with weak domestic fixed investment spending and is probably explained by domestic borrowing for investment into the rest of Africa.

The strong performance of the All Share index is in stark contrast to the anaemic state of the domestic economy, explained by the continuing surge in rand hedge stocks. The local equity market will continue to be driven by global markets and global monetary policy developments. The direction of the rand is key. In the medium-term

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the trajectory of the rand will mainly be dependent on global monetary policy events, the biggest being the timing of the normalisation of US interest rates. The extent to which this event has already been priced into the rand is unclear, but the general trend seems to be for a gradually weakening rand against the US dollar in 2015, which should provide further impetus to rand hedge stocks.

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