



OAM Local Real Return Portfolios
ZAR Rand

JAN 2015

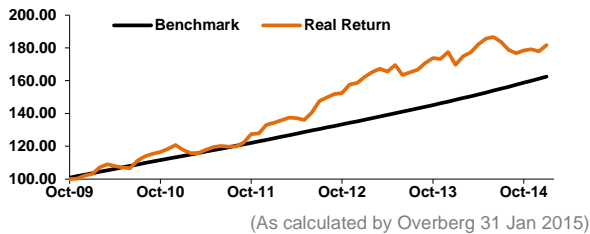
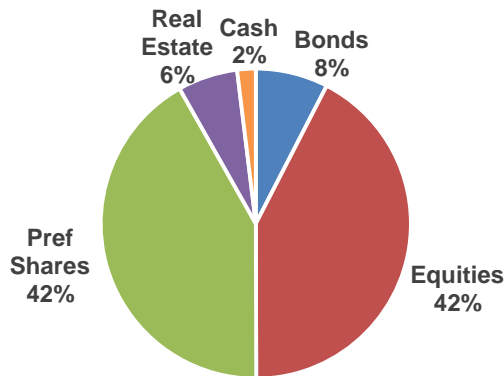
Technical Details

- 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

ASSET ALLOCATION



	Real Return %	Benchmark %
Annualised Total Return	12.05	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	2.16	0.77

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

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

		%
Annualised Income Yield		8.04



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 31 January 2015

With the exception of resource stocks SA equities enjoyed a strong fourth quarter (Q4) helped by a slight pick-up in the domestic economy and continued confidence in global equity markets. In 2014 the All Share Index increased 7.60%, although performance varied markedly across the different sub-indices. The Financial 15 Index led the way with a return of 22.72%, followed by the Industrial 25 Index which gained 14.45%. Unfortunately the Resource 10 Index lost a hefty -17.79% due to pricing weakness in commodity markets, and labour unrest in the platinum sector. Despite the labour unrest and government policy uncertainty the rand was relatively stable losing just -10.62% against the US dollar (the world's strongest currency in 2014). Bonds fared reasonably well as interest rates increased by less than expected. The All Bond Total return Index (1-3 year) returned 6.42% over the year. The gold price fell slightly in 2014 from \$1230 to \$1183, although the -3.82% decline was more than compensated by the resurgent dollar.

Recent indicators confirm that domestic economic conditions improved over Q3. The economy grew slightly faster expanding by an annualised 1.4% up from 0.5% in Q2, after shrinking in Q1 by -1.6%. The recovery was mainly driven by faster growth in "finance, real estate and business services", and in "wholesale, retail and motor trade, catering and accommodation" propped up by increased activity in financial markets. Agricultural output also accelerated further in Q3, boosted by a record grain harvest and higher livestock production. The biggest drag came from manufacturing which declined -3.4% due to the 4-week long NUMSA strike in July.

Provided the current power crisis does not worsen, the recovery is likely to continue and even accelerate moderately in the final quarter and into 2015. SA's manufacturing purchasing managers' index (PMI) rebounded strongly from 50.1 in October to 53.3 in November well above the key 50 threshold which demarcates expansion from contraction. Among the sub-indices the business activity index increased from 50.3 to a three-year high of 56.0 and the forward-looking new sales orders index from 50.2 to a 15-month high of 55.0. Meanwhile, the prices index fell from 76.0 to 67.8 reflecting a diminishing inflation threat as a result of lower oil prices. However, the expected business conditions index fell from 60.4 to 50.7 indicating that despite the overall improvement manufacturers were less optimistic about the outlook for the next six months. The main culprit is likely to be electricity supply interruptions. Nonetheless the buoyant headline PMI reading is consistent with an improvement in Q4 GDP growth to around 3.9% annualised.



The BER business confidence index also showed a marked improvement, albeit off a low base, increasing from 46 in Q3 to 51 in Q4 the first reading above the 50 threshold since Q1 2013. The improvement is attributed to large increases in the building and manufacturing sectors. The building index jumped from 50 to 66 its highest reading since 2008. The manufacturing index also jumped from 28 to 42. Although the retail index fell from 60 to 55 in response to the weak consumer spending climate the overall data is encouraging and consistent with a pick-up in fixed investment and improved GDP growth in Q4.

The country's trade deficit took an unexpected turn for the worse in October as oil imports surged, pushing total imports up by almost 18% month-on-month while exports fell by 1.8%. The trade deficit surged to -R21.3 billion, after shrinking to -R3.1 billion in September. The cumulative trade deficit for the first ten months of 2014 amounted to R95.1 billion, compared with R73.1 billion over the same period a year ago. The current account deficit is expected to average around -5.7% of GDP in 2014, before narrowing gradually in both 2015 and 2016 to just over -5% of GDP. Fortunately the continued decline in the oil price should reduce the import total in coming months given oil's 25% weighting in the import basket. Moreover, imports tend to be unusually high in October due to seasonal factors. As a result the trade deficit is likely to narrow significantly in November and December.

Credit demand improved in October. Growth in private sector credit extension increased from 8.7% in September to 9.1%. The biggest contribution came from loans to companies, which grew by 15.3% indicating an improvement in business activity and greater willingness for private sector investment. In contrast, loan growth to households moderated from 3.8% to 3.6% held back by weak employment growth, falling disposable income and elevated household debt levels. Demand for credit is still forecast to remain subdued, but should improve gradually off a low base throughout 2015.

Consumer price inflation (CPI) was steady at 5.9% in October marking the fourth month in 2014 that CPI has been within the SA Reserve Bank's 3-6% target range. The moderate inflation reading was led by food inflation which fell to a six-month low from 8.5% to 7.8%. CPI is expected to adjust downwards over coming months in response to recent sharp declines in agricultural commodity and oil prices. Although the outlook for inflation has improved, the rand remains a key risk. While the local unit has been surprisingly resilient over the past year, it remains intrinsically vulnerable given the country's twin deficits and the country's government policy uncertainty.

As expected the Reserve Bank Monetary Policy Committee (MPC), led by new Reserve Bank Governor Lesetja Kganyago, decided to keep interest rates on hold on 20 November, citing an improved inflation outlook. The MPC lowered its CPI forecast for 2015 from 5.7% to 5.3% which may moderate the extent of its monetary tightening this year. However, the MPC still believes "that interest rates will have to normalise over time". The benchmark repo rate is expected to increase during 2015 by between 50-100 basis points. The rand is anticipated to come under pressure once US interest rates start to rise around mid-2015, forcing the MPC to tighten policy more significantly in the second half of the year.

Minister of Finance Nhlanhla Nene presented his first Medium Term Budget Policy Statement (MTBPS) in October keeping to prudent fiscal policy in spite of lower forecasts for GDP growth. The Treasury's GDP growth forecast was lowered to 1.4% for 2014, 2.5% for 2015, rising slowly to 2.8% in 2016 and 3% in 2017. Encouragingly the fiscal deficit is forecast to decline to 4.1% of GDP in FY14/15, 3.6% in FY15/16 and 2.6% in FY16/17 an improvement on the previous forecast of 4.0%, 3.7% and 2.8%. The deficit reduction is premised on lowered government expenditure, to be achieved by linking growth in public sector compensation to inflation. Nene made encouraging statements, in particular acknowledging that SA's low economic growth is of our own making: "Energy constraints, labour market disruptions, skill shortages, administrative shortcomings and difficulties in our industrial transformation" were all cited.

Despite a fiscally prudent budget policy statement Moody's credit rating agency reduced SA's government debt rating by one notch from Baa1 to Baa2. Moody's cited "Poor medium-term growth prospects due to structural weaknesses, including ongoing energy shortages as well as rising interest rates, further deterioration in the investor climate, and a less supportive capital market environment for countries such as South Africa that are highly dependent on external capital." Moody's also remains skeptical that the Treasury's budget deficit



reduction plans will be achieved due to the low growth environment. Moody's highlights the prospect of further rises in the government debt-to-GDP ratio "which even strict compliance with the government spending ceiling and somewhat smaller fiscal deficits are unlikely to arrest in the near-term."

While electricity constraints are likely to limit SA's economic growth potential well into 2015 due to frequent episodes of load shedding, the lower oil price will provide an antidote, bringing numerous benefits: As a result of lower oil prices headline consumer price inflation is expected to fall sharply and due to lower expenditure on oil imports the current account deficit is also likely to improve materially from over 6% of GDP to around 4% of GDP. These macro-trends should enable the SA Reserve Bank to adopt a more accommodative monetary policy providing a boost to economic growth and financial markets. However, we are mindful that the current economic improvement is moderate and coming off a low base, susceptible to policy uncertainty, a vulnerable rand and weakness in SA's key trading partners, the Eurozone and China. In summary the economic outlook remains uncertain and the All Share Index is not especially cheap, remaining over-priced by around 15% on an estimated forward price to earnings multiple of 16x, compared with its 14x long-term average.