FLEXIPORTFOLIO

PERFORMANCE REPORT

1 DECEMBER 2017

SOUTH AFRICAN ECONOMIC REVIEW

Last month we alluded to Finance Minister Gigaba's rather shocking medium-term budget review, which saw a sharp deterioration in projected budget deficits over the next few years, effectively also putting paid to previous planned fiscal consolidation. These concerns were aggravated by rumours that the President was to announce free tertiary education (an outcome that would further pressure the already precarious fiscal situation) and the resignation of a senior official at National Treasury.

The immediate, and most important reaction to the medium-term budget was Standard & Poor's (S&P) ratings downgrade of South Africa's local government bonds to sub-investment grade. However, Moody's kept its investment grade rating unchanged, so preventing South Africa from being expelled from Citigroup's World Government Bond Index – an outcome that could have triggered large scale capital outflows and a severe hit on the rand.

In the immediate aftermath of the medium-term budget review, and following S&P's downgrade, the rand slumped to over R14.50/US$ at one point and the 10-year government bond yield (the rate at which government borrows money in the market) spiked to around 9.50%. A further result of the October events was that, at its November meeting, the South African Reserve Bank (SARB) maintained the more hawkish stance on monetary policy that it had already adopted at its September meeting. While the SARB left interest rates unchanged, it did indicate that inflation risks were now skewed to the upside – given the weaker rand, higher oil price and worsened fiscal outlook – and thus left no room for further rate reductions in the foreseeable future. In fact, the SARB's new integrated economic model now suggests three 25 basis point (bps) rate hikes through to the end of 2019. However, the SARB indicated that this outcome was merely indicative and that there is no unconditional commitment to such a rate profile.

Over the past month, the worst fears faded a bit again, causing the rand to retrace quite sharply to around R13.50/US$ by early December. Similarly, bond yields eased back to below 9.20%, although still well above the 8.5% before the medium-term budget review.

Two factors seemed to have been behind the calming of markets over the past month. The first was a firm indication from the Minister of Finance, supported by the Presidency, of a planned additional R40 billion, or some 0.9% of GDP, fiscal tightening in the 2018 Budget. While still only an undertaking, the markets assessed this as an indication that Government has not "given up" on containing the fiscal situation and that it is willing to take tough decisions in a difficult environment.

The second factor that helped lift sentiment was the confirmation early in December that the economy expanded by a further 2% annual rate in the third quarter, following an upwardly revised 2.8% in the second quarter. While overall growth for the full calendar year is still below 1% (our forecast is 0.9%), it did send a message to investors that the economy has not entered a full-blown slump – given the deeply depressed business, investor and consumer confidence – and has raised hopes that the commonly forecast improvement in the economy in 2018 is indeed possible, especially if confidence was to lift a bit after the ANC's elective conference in December.

Looking into 2018, we continue to expect a moderate improvement in economic growth to around 1.5%, largely driven by improved net exports. Failing a material improvement in confidence, it is difficult to see private investment recover, while consumers will face further headwinds from fiscal tightening (likely considerable tax hikes), little interest rate relief and little, if any, employment growth.

So, while prospects look anything but rosy for 2018, it is worth remembering that a material, politically driven, improvement in confidence can pay considerable and quick economic dividends, an outcome we are not only hoping for, but one that South Africa is in urgent need of.

MARKET PERFORMANCE INCLUDING DIVIDENDS

	LAST MONTH (%)	YEAR TO DATE (%)	1 YEAR (% P.A.)	3 YEARS (% P.A.)	5 YEARS (% P.A.)	8 YEARS (% P.A.)	10 YEARS (% P.A.)
JSE All Share	1.5	21.4	22.5	9.3	12.7	13.8	10.2
JSE Fin & Ind	2.3	22.3	25.2	10.4	16.4	19.0	14.7
JSE Resources	-1.6	18.4	14.2	-1.5	-2.3	-0.5	-1.6
ALSI 40	1.4	24.7	25.4	9.5	12.7	13.4	9.8
All Bond	-1.0	4.3	6.0	4.4	5.6	8.2	8.1
Cash	0.6	6.9	7.6	7.1	6.5	6.3	7.2

RETIREMENT ANNUITIES TO 01/12/2017 (REFER NOTES)

	PERFORMANCE PROFITS									SMOOTHED BONUS			STABLE FUND			CPI
	Equity %			Balanced %			Select %			%			%			
Period	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	%
1 Year	22.1	17.7	17.7	14.6	12.3	12.3	18.6	14.7	14.7	9.5	9.4	9.4	6.3	6.3	6.3	4.8
2 Years	12.1	10.1	6.6	9.4	8.4	6.6	10.6	8.2	5.1	9.2	9.2	9.1	6.3	6.2	6.2	5.6
3 Years	9.0	8.6	7.2	8.0	8.0	7.6	7.9	7.8	7.4	9.4	9.6	10.0	6.1	6.0	5.8	5.3
5 Years	9.6	10.3	12.4	8.9	9.3	10.8	8.7	9.2	10.8	10.8	11.1	12.3	5.6	5.5	5.0	5.5
8 Years	11.7	11.8	12.3	10.4	10.4	10.7	10.3	10.3	10.6	11.4	11.4	11.1	5.1	5.1	4.8	5.3
10 Years	11.6	11.3	8.2	10.2	10.0	8.3	10.2	10.0	7.8	11.0	11.0	10.3	5.1	5.2	5.5	6.0
15 Years	12.3	12.3	13.2	10.8	10.7	11.4	11.0	11.0	12.0	11.6	11.6	11.7	5.4	5.4	5.7	5.7
20 Years	12.4	12.4	12.2	10.8	10.9	10.8	-	-	-	11.4	11.3	10.9	5.6	5.6	6.2	6.2
25 Years	12.3	12.6	13.8	10.9	11.1	12.0	-	-	-	11.4	11.4	11.8	6.4	6.5	7.8	6.6
INTERIM RATES										9.50% p.a. (0.759% p.m.)			0.509% p.m.			

ENDOWMENTS/LIFE PORTFOLIOS TO 01/12/2017 (REFER NOTES)

	PERFORMANCE PROFITS									SMOOTHED BONUS			STABLE FUND			CPI
	Equity %			Balanced %			Select %			%			%			
Period	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	%
1 Year	17.6	13.7	13.7	12.5	10.4	10.4	15.1	11.7	11.7	8.0	7.9	7.9	3.6	3.6	3.6	4.8
2 Years	9.2	7.3	4.3	7.8	6.8	5.1	8.2	6.0	3.4	7.7	7.7	7.6	3.7	3.6	3.6	5.6
3 Years	6.8	6.4	5.6	6.6	6.5	6.2	6.0	5.9	5.7	7.9	8.1	8.5	3.6	3.5	3.4	5.3
5 Years	8.0	8.6	11.2	7.5	7.9	9.5	7.1	7.5	9.5	9.3	9.5	10.8	3.3	3.2	2.8	5.5
8 Years	10.5	10.6	11.5	9.0	9.0	9.2	9.0	9.0	9.6	9.9	9.9	9.7	2.9	2.9	2.7	5.3
10 Years	10.5	10.3	7.3	8.8	8.6	6.9	9.0	8.8	6.8	9.6	9.5	8.9	3.0	3.1	3.5	6.0
15 Years	11.2	11.2	12.1	9.3	9.3	10.1	9.7	9.8	10.9	10.3	10.3	10.6	3.4	3.5	4.0	5.7
20 Years	11.2	11.3	11.1	9.5	9.6	9.6	-	-	-	10.2	10.2	10.0	3.9	4.0	5.0	6.2
25 Years	11.2	11.5	12.6	9.6	9.8	10.7	-	-	-	10.3	10.4	10.8	4.8	4.9	6.2	6.6
INTERIM RATES										8.00% p.a. (0.643% p.m.)			0.296% p.m.			

GUARANTEED CAPITAL FUND (CURRENT AFTER-TAX RATE)		4.90% p.a. (0.399% p.m.)
EQUIVALENT RETURN	at the tax rate of 18%	5.98% p.a. (0.485% p.m.)
	at the tax rate of 41%	8.31% p.a. (0.667% p.m.)

PORTFOLIO ASSET SPLIT

	RETIREMENT ANNUITIES						ENDOWMENTS/LIFE					
	PP Equity %	PP Balanced %	PP Select %	Smoothed Bonus %	WW Equity %	WW Balanced %	PP Equity %	PP Balanced %	PP Select %	Smoothed Bonus %	WW Equity %	WW Balanced %
Interest-bearing	0 (0)	27 (3)	0 (0)	25 (0)	0 (0)	27 (27)	0 (0)	26 (3)	15 (0)	25 (0)	0 (0)	27 (27)
Ordinary Shares	100 (25)	66 (30)	75 (27)	66 (24)	100 (85)	73 (58)	100 (25)	67 (30)	75 (27)	66 (24)	100 (86)	73 (58)
Property	0	7	10	7	0	0	0	6	0	7	0	0
Other	0	1	0	2	0	0	0	1	0	2	0	0

Figures in brackets — international portion of sector weighting

TOP EQUITY HOLDINGS (SA)

NAME		% SPLIT	SECTOR
1.	Naspers Ltd	14.5	Media
2.	British American Tobacco	5.4	Consumer Goods
3.	Sasol	4.7	Oil & Gas
4.	Standard Bank	3.7	Banks
5.	Barclays Africa	3.5	Banks
6.	Steinhoff International Holdings	3.4	Personal & Household Goods
7.	Old Mutual	3.0	Financials
8.	MTN	2.8	Telecommunications
9.	FirstRand	2.6	Banks
10.	Remgro	2.3	Financials

GLOBAL ECONOMIC OVERVIEW

Recent data across most of the world's major economies showed evidence of continued strong growth trends. The latest Purchasing Managers Indexes (PMIs) were especially strong across Europe and Asia. The JP Morgan proprietary Global Manufacturing PMI (a weighted aggregate index from individual country PMIs) rose to the highest level in seven years. In addition to this strong level of activity in the manufacturing sectors, global capital expenditure is also turning more expansionary on the back of tighter capacity rates as manufacturers try to keep up with demand.

Meanwhile, the circular feedback from strong growth to improved sentiment and supportive financial conditions remains very strong. Global equity prices have moved a lot stronger this quarter, while bond yields remain largely unchanged. As a result, consumer confidence has moved stronger still – to the best levels in many years. It thus seems that the global economy is firing on all cylinders at present.

Make no mistake, though, the uptick in energy prices and food inflation during the second half of this year will likely lead to some slowing in the recent strong growth pace. This is not expected to be a sharp or sustained slowing, though, as the tailwinds of positive confidence and supportive financial conditions are markedly stronger than the headwinds of recent increases in energy and food prices.

2018 is expected to be another year of strong and synchronised global growth. It is likely that most developed economies will show steady growth – with the possible exception of the Euro area, where growth could actually accelerate. Emerging markets should also see stronger growth in 2018 than in 2017. Thus, the current growth cycle will be extended with little serious risk of a downturn in the global economy.

Inflation is still low and very much under control in the major economies. However, this is likely to change into 2018. While headline inflation rates in the developed economies should largely move sideways, core inflation will likely move higher. Despite many economies at, or close to, full employment levels (that is, the US, Germany and Japan), this lift in core inflation is unlikely to be enough to breach central banks' target levels. Inflation in emerging economies will also move higher over the next year. We do not expect runaway inflation anywhere.

In the US, the Federal Reserve Board (the Fed's) preferred inflation measure, the core PCE deflator, is currently at 1.4%. This is markedly below the 2% target that the Fed has set. With wage growth at a much lower than anticipated pace at this stage of the business cycle (presently around 2.5%), there is no serious risk of core inflation breaching the target in the medium term.

Thus central banks are set to continue policy normalization at a slow pace. In the US, this means slow and steady increases in the policy interest rate. The Fed is expected to hike rates again in December and three (or four) more times in 2018. Simultaneously, it continues on a slow and measured process of running down its US$4.5 trillion balance sheet.

The conditions for strong equity market performance thus remain in place. As highlighted last month, these include strong global growth and policy normalisation as a sign of policymakers' growing confidence that the global recovery is becoming self-sustaining, thus requiring less monetary support.

Potential central bank policy error remains a risk. In the face of an acceleration in inflation, even if only modest, central banks might move rates up faster than market expectations. Markets also look forward, so might become worried about slower growth later in 2018 and into 2019.

GLOBAL MARKET PERFORMANCES IN RAND TERMS

	LAST MONTH (%)	YEAR TO DATE (%)	1 YEAR (% P.A.)	3 YEARS (% P.A.)	5 YEARS (% P.A.)	8 YEARS (% P.A.)	10 YEARS (% P.A.)
MSCI World	-1.4	21.1	20.9	16.7	22.5	19.2	13.0
JP Morgan	-2.3	6.4	3.1	9.1	9.0	9.4	10.3
S&P 500	-0.6	20.2	19.5	19.0	26.1	23.0	16.0
FTSE 100	-3.4	16.5	18.4	9.3	14.3	14.1	8.2
Nikkei Index	1.1	23.6	22.9	19.5	22.2	16.7	11.2
Rand/Dollar	-3.5	-0.2	-2.7	7.3	9.0	7.9	7.2

WORLDWIDE FUNDS: PERFORMANCE IN RAND TERMS – REFER NOTES

	WW EQUITY %						WW BALANCED %					
	Retirement Annuities			Endowments/Life			Retirement Annuities			Endowments/Life		
Period	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.
1 Year	29.7	23.0	23.0	25.4	19.5	19.5	24.3	17.5	17.5	20.6	14.5	14.5
2 Years	16.6	14.1	10.1	14.2	12.0	8.5	11.8	10.5	7.3	9.8	8.5	5.7
3 Years	14.5	14.1	14.2	12.8	12.5	12.9	11.4	11.9	13.2	9.7	10.2	11.6
5 Years	15.0	15.7	18.2	13.7	14.3	17.1	12.8	13.6	15.7	11.4	12.1	14.6
8 Years	16.5	16.1	14.6	15.5	15.1	13.9	14.5	14.1	13.0	13.4	13.1	12.3
10 Years	14.5	13.8	8.4	13.6	12.9	7.6	12.9	12.4	8.8	12.0	11.5	8.1
15 Years	11.4	11.3	9.0	10.5	10.3	7.8	11.0	10.8	8.7	10.1	9.9	7.7

GEOGRAPHICAL SPREAD

	EQUITY PORTION %			BOND PORTION %		
	Fund	MSCI	Difference	Fund	Benchmark[7]	Difference
United States	40.4	52.6	-12.2	35.5	38.4	-2.8
Japan	4.0	8.0	-3.9	3.2	16.9	-13.7
Europe ex UK	20.4	15.6	4.8	31.4	28.7	2.7
United Kingdom	7.5	5.7	1.8	8.7	5.6	3.1
SE Asia & Canada	9.4	12.0	-2.6	14.5	8.4	6.0
South Africa	14.5	0.0	14.5	0.0	0.2	-0.2
Other	3.8	6.1	-2.3	6.7	1.8	4.9
Total	**100.0**	**100.0**	**0.0**	**100.0**	**100.0**	**0.0**

EQUITY SECTOR SPREAD

	Fund	MSCI	US	JAPAN	UK	Europe ex UK
Cash	2.0	0.0	0.9	0.1	0.2	0.5
Consumer Discretionary	9.0	12.1	4.2	0.4	0.8	2.1
Consumer Staples	6.6	8.7	3.1	0.3	0.6	1.6
Energy	4.8	6.2	2.3	0.2	0.4	1.2
Financials	17.7	18.6	8.4	0.8	1.6	4.2
Healthcare	10.7	10.9	5.1	0.5	0.9	2.6
Industrials	11.2	10.7	5.3	0.5	1.0	2.7
Information Technology	14.3	18.2	6.8	0.7	1.3	3.4
Materials	5.1	5.3	2.4	0.2	0.4	1.2
Other	0.2	0.0	0.1	0.0	0.0	0.1
Telecoms Services	0.6	3.0	0.3	0.0	0.1	0.1
Utilities	1.8	3.1	0.8	0.1	0.2	0.4
SA Rand Hedge	14.5	0.0	0.0	0.0	0.0	0.0

TOP EQUITY HOLDINGS (GLOBAL)

NAME	SECTOR
1. JPMorgan Chase & Co	Financials
2. Moody's Corporation	Financials
3. Fiat Chrysler Automobiles	Consumer Discretionary
4. Pepsico Inc	Consumer Staples
5. Keyence Corporation	Information Technology
6. Bank of America Corporation	Financials
7. DS Smith Plc	Materials
8. Alphabet Inc	Information Technology
9. Mastercard Inc	Information Technology
10. Johnson & Johnson	Healthcare

NOTES

1. The performance figures in the tables represent the returns earned on premiums allocated. The returns on premiums actually paid will be lower than this because they take the policy specific charges into account.

2. All returns are quoted net of investment fund charges and tax.

3. The Smoothed Bonus declaration is made up of a vesting bonus and a claim bonus. The vesting bonus portion of the total bonus cannot be removed on death or maturity of the policy. The claim bonus portion is not guaranteed and could be adjusted should investment conditions dictate.

4. M.P. = monthly premium, A.P. = annual premium, S.P. = single premium.

5. The Flexi range of products was launched on 1 September 1984. Returns for the periods starting before this date apply to policies available before the introduction of the Flexi range of products.

6. The Property Portfolio and the OMD Top 40 Index Fund returns are available at any time.

7. The MSCI World Index is the benchmark for the Worldwide Equity portion. The benchmark figures for the Worldwide Bond portion consist of 70% JP Morgan Bond Index and 30% Barclays Capital Global Bond Index.

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