FLEXIPORTFOLIO

PERFORMANCE REPORT

1 JUNE 2017

SOUTH AFRICAN ECONOMIC REVIEW

The rand has continued to hold up surprisingly well since the replacement of Finance Minister Pravin Gordhan with Malusi Gigaba. This is largely because of sustained flows into the local bond market from offshore investors and a notably smaller foreign financing deficit (as a result of a smaller deficit on the current account of the balance of payments). The rand got a renewed boost early in June when both Fitch and Standard & Poor's (S&P) left their respective ratings of SA's foreign and local currency bonds unchanged.

As a reminder, Fitch has both ratings at the highest level of sub-investment grade, while S&P has SA's sovereign rating at the highest level of sub-investment grade, but the local currency bonds at the lowest level of investment grade. Moody's rating review, which, at the time of writing, is currently at two levels into investment grade for both the local and sovereign ratings, investors remained convinced that it will not effect more than a one notch downgrade when the outcome of the review is announced in early June. Such an outcome will leave the local currency bond at investment grade for both S&P and Moody's and will leave SA's membership of Citibank's huge World Government Bond Index intact (read Zain's article on page xx for more on this). As a result, the rand firmed further and was trading at R12.75 against the US dollar in early June.

On the economic front, incoming data pointed to sustained weak overall economic activity – with car and retail sales, building plans passed, credit demand and manufacturing production all remaining weak at the end of the first quarter. On a more positive note, mining production surged in the first quarter, although it is questionable whether this can be sustained in the second quarter, and a strong recovery in agricultural production is under way with summer grain crops almost double the output of the previous season. The surge in mining production and the prospective strong recovery in agricultural output was, however, not enough to prevent yet another round of growth forecast downgrades for 2017. Consensus GDP forecasts are now bunched around 1% for this year, with a number of forecasters predicting less than 1% growth. While still better than the 0.3% recorded in 2016, it remains a poor performance, given that SA requires a far faster growth rate to reverse the 27% unemployment rate.

Another piece of good news over the past month was another downside surprise in inflation, with headline inflation falling from 6.1% in March to 5.3% in April and the core inflation (CPI excluding food and energy) easing slightly further to only 4.8%. Should the rand stay around early-June levels over the next two months, and oil remains around US$50 a barrel, headline inflation could fall to about 4.7% by July, an outcome that will bring us very close to a rate cut by the South African Reserve Bank (SARB). We therefore stay with our view held since mid-2016 that conditions will be favourable by the second half of 2017 for the SARB to start with a slow process of easing monetary policy. From a macroeconomic perspective, these conditions are fast falling into place. However, political and policy uncertainty around the ANC's mid-year policy conference and its end of year elective conference, could potentially still trip up the rand – a possible outcome that is clearly the key obstacle for the SARB to consider lowering rates at this stage.

In summary, the rand has undeniably surprised almost everyone with its robust behaviour since the shock removal of previous Finance Minister Gordhan. The likely key reasons for this were strong capital flows to emerging markets, SA managing to hang on to its investment grade rating on local bonds from two of the three key rating agencies, a small foreign financing shortfall and still high local interest rates.

Unfortunately, the outlook for the rand, the economy and interest rates remains clouded by political risk over the remainder on the year. So, while 2017 will undoubtedly be another year of growth disappointment, one can only hope that 2018 will bring greater clarity as to the direction of economic policy and a growth-enhancing recovery in business, consumer and investor confidence.

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	-0.4	6.9	8.1	5.6	13.4	14.5	9.6
JSE Fin & Ind	0.6	4.3	12.2	9.6	18.3	20.5	13.8
JSE All Gold	-1.9	19.9	-4.7	0.9	-11.2	-7.7	-5.6
All Bond	1.0	14.5	6.6	7.8	7.5	8.7	8.3
Total Cash	0.6	6.8	3.4	6.0	5.5	5.5	6.5
ALSI 40	0.2	4.9	9.3	4.8	13.3	14.0	9.3
INDI 25	1.8	4.1	17.7	10.8	21.1	22.9	16.8

RETIREMENT ANNUITIES TO 01/06/2017 (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	7.7	-0.5	7.8	6.7	2.1	5.5	4.0	-0.7	5.0	7.9	8.1	3.8	6.4	6.4	3.1	2.9
2 Years	5.1	1.6	2.6	5.8	4.0	5.0	3.1	0.8	1.5	8.4	8.8	9.2	6.2	6.1	5.9	5.7
3 Years	4.8	3.7	5.6	6.0	5.6	7.1	4.0	3.3	5.7	9.3	9.7	10.5	5.9	5.8	5.6	5.3
5 Years	8.7	8.8	12.9	8.6	8.8	11.5	7.4	7.5	11.0	11.1	11.3	12.3	5.3	5.2	4.8	5.6
8 Years	11.1	11.4	13.3	10.2	10.3	11.3	9.4	9.7	11.2	11.4	11.3	10.9	4.9	4.9	4.8	5.4
10 Years	10.5	9.9	7.5	9.7	9.4	7.8	9.2	8.8	7.1	11.0	10.9	10.5	5.1	5.1	5.5	6.1
15 Years	12.0	11.8	11.6	10.6	10.5	10.2	10.7	10.6	11.0	11.6	11.6	11.4	5.4	5.4	5.7	5.6
20 Years	12.1	11.8	11.4	10.7	10.6	10.4	-	-	-	11.3	11.3	10.8	5.6	5.7	6.4	5.7
25 Years	12.4	12.2	12.5	10.9	10.9	11.4	-	-	-	11.4	11.5	11.9	6.5	6.6	8.0	6.3
INTERIM RATES										9.50% p.a. (0.759% p.m.)			0.522% p.m.			

ENDOWMENTS/LIFE PORTFOLIOS TO 01/06/2017 (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	5.9	-1.5	6.3	5.5	1.3	4.7	2.6	-1.5	3.8	6.4	6.6	3.0	3.7	3.7	1.8	2.9
2 Years	3.6	0.7	1.8	4.5	3.0	3.8	1.8	-0.2	0.5	6.9	7.3	7.7	3.6	3.6	3.5	5.7
3 Years	3.7	2.7	4.6	4.8	4.5	5.9	2.7	2.2	4.3	7.8	8.2	9.0	3.5	3.4	3.3	5.3
5 Years	7.7	7.9	12.0	7.3	7.4	10.1	6.1	6.3	9.7	9.6	9.8	10.8	3.1	3.0	2.7	5.6
8 Years	10.3	10.7	12.7	8.8	8.9	9.8	8.4	8.6	10.2	9.9	9.8	9.5	2.8	2.8	2.8	5.4
10 Years	9.8	9.2	6.7	8.3	8.0	6.5	8.1	7.8	6.2	9.5	9.5	9.2	3.0	3.1	3.6	6.1
15 Years	11.1	10.9	10.4	9.2	9.1	9.0	9.5	9.5	10.0	10.3	10.3	10.3	3.5	3.5	4.1	5.6
20 Years	11.1	10.9	10.5	9.4	9.3	9.2	-	-	-	10.2	10.2	9.9	4.0	4.1	5.2	5.7
25 Years	11.4	11.2	11.5	9.6	9.6	10.2	-	-	-	10.4	10.4	10.8	5.0	5.1	6.4	6.3
INTERIM RATES										8.00% p.a. (0.643% p.m.)			0.300% p.m.			

GUARANTEED CAPITAL FUND (CURRENT AFTER-TAX RATE)		4.70% p.a. (0.383% p.m.)
EQUIVALENT RETURN	at the tax rate of 18%	5.73% p.a. (0.466% p.m.)
	at the tax rate of 41%	7.97% p.a. (0.641% 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 (2)	13 (0)	25 (0)	0 (0)	26 (26)	0 (0)	27 (2)	13 (0)	25 (0)	0 (0)	26 (26)
Ordinary Shares	100 (25)	65 (30)	77 (27)	66 (24)	100 (85)	74 (59)	100 (25)	66 (30)	77 (27)	66 (24)	100 (85)	74 (59)
Property	0	7	10	7	0	0	0	7	10	7	0	0
Other	0	1	0	2	0	0	0	1	0	1	0	0

Figures in brackets — international portion of sector weighting

TOP EQUITY HOLDINGS (SA)

NAME		% SPLIT	SECTOR
1.	Naspers Ltd	20.4	Media
2.	British American Tobacco	5.0	Consumer Goods
3.	Sasol	4.2	Oil & Gas
4.	Steinhoff International Holdings	4.0	Industrials
5.	Standard Bank	2.9	Banks
6.	Old Mutual	2.6	Life Insurance
7.	Remgro	2.5	Industrials
8.	MTN	2.3	Telecommunications
9.	Aspen Pharmacare Holdings Limited	2.3	Pharmaceuticals
10.	Barclays Africa	2.1	Banks

GLOBAL ECONOMIC OVERVIEW

The past month was relatively quiet on the global front, although three issues caught investors' attention.

The first issue was a tightening in the regulatory environment by Chinese authorities around credit extension, the goal being to accelerate the debt deleveraging process. Private sector debt, both corporate and household, has risen very sharply in recent years and has, for some time now, been regarded as a key risk to the Chinese economy. Focusing on the rising risks associated with the debt build-up, Moody's downgraded China's sovereign and local debt ratings by one notch, although both remain six levels (out of a maximum of ten) into investment grade. Still, as the first ratings downgrade since 1989, it increased the focus on debt risks, while the intensified regulatory tightening, a process the Chinese authorities strongly indicated will remain in place for some time, caused some concern over the medium outlook for the economy. In its review of the economy, Moody's indeed concluded that growth in China will average only about 5% a year over the next five years, notably below the common view of growth being sustainable at about 6.5% a year. As such, the recent fading concerns about the outlook for the Chinese economy turned into a bit more uncertainty and concern again.

The second issue that was worth noting over the past month was a general softening of concerns over the extent of US Federal Reserve tightening this year. While the Fed itself signaled that it will raise the policy rate again soon, and start with a very gradual process of reducing its sizeable holdings of US government debt and other debt securities, incoming economic data has been mostly softer than expected and inflation has actually surprised on the downside. Hence, market conclusions were that, while another hike may indeed be imminent, previous concerns over the Fed possibly being "behind the curve" with rate hikes and that they may be forced to speed up the pace of tightening later this year, have all but faded away again. Nowhere is this better reflected in the US 10-year Treasury yield, which ended the month at 2.20%, well down from the 2.6% reached in mid-March. In addition, the US dollar softening further, reaching US$1.1 to the euro by the end of May, well off the US$1.04/€ in December 2016.

The third notable global issue in May was a renewed fall in the oil price to around US$50 a barrel by the end of the month, down from US$55 in the middle of April –a level where it traded most of the year so far. The trigger for renewed oil price weakness was ironically a decision by OPEC to extend by a further nine months a deal to reduce oil production by its members. The original deal, to reduce production by 1.8 million barrels a day between January and June 2017, was reached in December 2016 and helped oil to bounce from around US$45 to US$55 a barrel. While members complied with the targeted output cuts, it failed to reduce global oil inventories much, as US shale production surged – offsetting a fairly large part of the OPEC cutbacks. As a result, the extension of the oil deal caused the price to slide as analysts' concluded that a greater cutback was required, or more non-OPEC countries had to join the deal to achieve the desired effect. Moreover, history has shown that compliance tends to weaken as time passes.

Meanwhile, global growth has remained fairly buoyant, with better data from the Eurozone and emerging markets more than offsetting soft US growth numbers. The world remains in a synchronized recovery and with little inflation risk, policy settings will likely remain growth supportive over the remainder of the year.

We ended last month's review with the same conclusion as above, namely that the global economy remains on a relatively solid footing and there is growing confidence that the world has finally entered a period of synchronised, even though still sub-par, growth. Nevertheless, we argued that there were still a number of risks that could not be ignored, the most important of which are the mounting debt problems in China and a flare-up in geopolitical tensions. Chinese developments over the past month indeed indicated that, while global confidence is relatively high at present, there are always risks that should be carefully considered by investors.

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	0.7	1.2	6.5	14.4	23.2	18.9	11.1
JP Morgan	0.0	-7.1	-2.6	7.4	9.0	8.8	10.4
S&P 500	-0.1	2.5	4.2	18.5	25.8	22.5	13.6
FTSE 100	3.1	-3.4	9.8	5.7	17.1	14.7	7.2
Nikkei Index	1.7	-3.1	4.0	15.5	20.2	14.3	8.4
Rand/Dollar	-1.5	-10.8	-6.0	7.6	9.0	6.4	6.4

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	10.1	-3.1	7.3	8.7	-2.6	6.3	4.2	-7.6	4.4	3.5	-7.2	3.7
2 Years	7.2	4.0	7.3	6.4	4.0	7.0	3.6	1.9	6.5	3.0	1.6	5.8
3 Years	8.9	7.7	10.9	8.3	7.3	10.3	7.0	6.3	10.1	6.1	5.6	9.2
5 Years	13.2	13.0	17.7	12.5	12.6	17.0	11.3	11.2	15.3	10.5	10.5	14.5
8 Years	14.8	14.5	14.6	14.2	14.0	13.9	13.0	12.8	12.8	12.4	12.2	12.3
10 Years	12.4	11.5	6.2	11.8	11.0	5.6	11.2	10.6	7.1	10.7	10.1	6.6
15 Years	10.2	9.6	6.6	9.4	8.8	5.3	9.9	9.5	6.7	9.2	8.8	5.9

GEOGRAPHICAL SPREAD

	EQUITY PORTION %			BOND PORTION %		
	Fund	MSCI	Difference	Fund	Benchmark[7]	Difference
United States	44.2	52.6	-8.4	33.6	38.6	-5.1
Japan	3.8	7.7	-3.9	4.0	17.6	-13.6
Europe ex UK	18.6	16.1	2.5	34.7	27.9	6.8
United Kingdom	6.5	6.0	0.5	6.8	5.6	1.2
SE Asia & Canada	9.0	11.7	-2.6	17.1	8.4	8.8
South Africa	14.5	0.0	14.5	0.0	0.2	-0.2
Other	3.4	6.0	-2.6	3.9	1.7	2.1
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	3.5	0.0	1.8	0.2	0.3	0.8
Consumer Discretionary	8.7	12.3	4.5	0.4	0.7	1.9
Consumer Staples	7.4	9.7	3.8	0.3	0.6	1.6
Energy	4.0	6.2	2.0	0.2	0.3	0.9
Financials	15.5	17.9	8.0	0.7	1.2	3.4
Healthcare	10.6	11.2	5.5	0.5	0.8	2.3
Industrials	12.1	10.8	6.3	0.5	0.9	2.6
Information Technology	13.8	17.1	7.2	0.6	1.0	3.0
Materials	5.0	5.2	2.6	0.2	0.4	1.1
Other	0.4	0.0	0.2	0.0	0.0	0.1
Telecoms Services	1.5	3.4	0.8	0.1	0.1	0.3
Utilities	1.4	3.2	0.7	0.1	0.1	0.3
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.	Oracle Corporation	Information Technology
3.	CRH Plc	Materials
4.	Alphabet Inc	Information Technology
5.	Citigroup Inc	Financials
6.	Moody S Corp	Financials
7.	Fiat Chrysler Automobiles	Consumer Discretionary
8.	FMC Corp	Materials
9.	Apple Inc	Information Technology
10.	Owens Corning	Industrials

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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