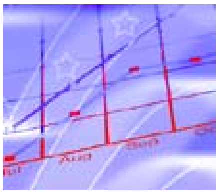
It is all in the Outcome

Anil Thakersee, MD, Old Mutual Unit Trusts



The South African unit trust industry was established in 1965, some 78 years after the Johannesburg Securities Exchange (JSE) first opened its doors on the corner of Commissioner and Simmonds Streets. Unit trusts gave South Africans access to a portfolio of shares from as little as R10 a month.

The first unit trusts on offer were general equity funds, investing across all sectors of the JSE. Next came single-sector funds, namely gold and industrial funds, and then income funds. It was only in the 1990s that the industry really took off, with investors being given a wider choice of funds – from bond to asset allocation funds, money market and property funds. And then, of course, came the global funds.

After 35 years of delivering unit trusts that offered access to the stock and interest income markets, the last five years have seen a new trend evolve. This is the shift from relative performance funds to funds focusing on specific investor needs – also referred to as **outcome-based** funds. The distinction can be seen in what a fund aims to deliver to an investor:

- Relative performance funds aim to beat either their benchmark or their peers, regardless of the performance. An extreme example of this would be our Gold Fund. It aims to outperform the FTSE/JSE Gold Mining Index regardless of whether it delivers -37.5% p.a. (to year ending 31/12/1997) or 79.8% p.a. (to year ending 31/12/2001).
- Outcome-based funds focus on a specific outcome and not on the performance of a benchmark. This outcome can be a performance objective (e.g. aiming to beat inflation by a set percentage) or a risk objective (e.g. aiming to avoid capital losses over a 12-month period).

This is not just a local trend: research by McKinsey & Company in the USA has shown that consumers exhibit a strong willingness to purchase outcome-based mutual funds (unit trusts). In recent years the annual growth rate of these funds in the USA has been over twice that of traditional funds. "We believe that successful firms of the future will break away from the pack and offer fewer products... winning players will expand the definition of 'asset class' by marketing specific outcomes, such as target retirement dates, tax minimization and income generation."

The Asset Management Industry in 2010. McKinsey & Company.

A similar trend can be seen in South Africa, with outcome-based funds now attracting the majority of new money flowing into the unit trust industry.

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IN THIS ISSUE

From the Editor

Tracy Hennessy,
Head of Communications

For many the new year is a good time to turn over a new leaf and we decided to do just that, literally. I hope you like Financially Talking's new layout.

Onto matters of the market... did you know that South African shares have experienced a bull market for the last 15 quarters (to end of December 2006)? This is undoubtedly one of the longest bull markets since the 1960s. It is therefore not surprising that our fund managers are cautioning investors to expect lower returns from equities (shares) than what they have become accustomed to over the last four years. They further anticipate the equity market to be more volatile in the year ahead.

In this edition of Financially Talking we have some useful information on our funds – especially those that focus on risk management (refer to the table on page 5). Also of interest is the introduction of a new measure to evaluate costs deducted from your investments. Read more about this on page 7.

Enjoy this edition of Financially Talking.

Regards

Tracy

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Important fund information

With approval from investors and the Financial Services Board (FSB), we have merged the Industrial Fund with the Financial & Industrial Fund. These funds had similar investment mandates, with the latter including financial shares. Given that we have a Financial Services Fund, and that the Financial & Industrial Fund was the only remaining unit trust in its category, we decided to seek investor approval to merge this fund with the Industrial Fund.

Financial & Industrial Fund clients received new account numbers and units to the equivalent value in the Industrial Fund (Class R).

Focusing on the outcome: Dynamic Floor Fund

Old Mutual's Dynamic Floor Fund has been on offer since November 2002. Financially Talking speaks to Portfolio Manager Garth Taljard about how his fund works and how he responds to different market conditions.

FT: What does this fund offer investors?

Garth: The fund aims to profit from a rising share market and to protect your capital in a weak market. Its investment objective is two-fold: Firstly, to provide you with inflation (CPI) plus 4% per annum over rolling 3-year periods and, secondly, to limit capital losses to no more than 10% of your net investment amount over any 12-month period.

FT: This fund has attracted over R1.1 billion from investors over the last year – how do you invest all this money?

Garth: I use a quantitative risk model to actively allocate money between various asset classes – that is shares, property, bonds and cash. I then adjust this allocation to take advantage of changing market and economic conditions. That way I work towards growing investors' money.

I am also fortunate in that I can draw on Old Mutual's in-house research, stockpicking capabilities and asset allocation expertise when making investment decisions.

FT: What do you do to protect investors' money?

Garth: I use what I call a "forward floor" to protect investors from losing more than 10% of their net investment over any 12-month period. The floor is set at 90% of the fund's value in 12 month's time. The floor level is a target, and is not guaranteed. This example may help explain how the floor works:

Had you invested R100 000 on 1 January 2006 your "forward floor" for the end of December would have been R90 000 (90% of R100 000). However, by the end of December the investment was actually worth R110 258. Your floor for the next 12 months would now be 90% of R110 258 (i.e. R99 232) and so you climb, steadily.
(Note: This example excludes costs.)

FT: What happens when the stock market crashes?

Garth: If markets start to fall and the fund value approaches its floor, using the quantitative model, I will protect the floor by moving from shares into cash and money market instruments. However, if at this

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Meet Old Mutual Unit Trusts' (new) MD

Anil Thakersee, our new Managing Director, needs little introduction to many of you as he has long been a contributor to Financially Talking.

Anil has been with Old Mutual Unit Trusts for five years in various senior roles covering marketing, business development and strategy. He was also Head of Investment Marketing for Old Mutual (SA) and responsible for the front-office Treasury operations for Old Mutual Bank.

Prior to joining Old Mutual, he was a fund manager of multi-manager funds and Treasury dealer at Appleton Asset Management and BoE Private Bank respectively. He began his career at First National Bank as a management trainee in their International and Treasury division.

Anil has a BCom degree in economics and is a CFA charterholder.

While passionate about his industry and investment markets, Anil sees an important part of his role as being a champion for his clients. He regularly interacts with and meets clients and is always willing to listen to their views and opinions.

A family man at heart, Anil believes spending time with his wife Tanya and his two-year-old son Pranay to be a top priority in his busy schedule.

Focusing on the outcome: Dynamic Floor Fund

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point the market rises strongly and quickly, the fund will not be positioned to fully participate in the upward movement. This is because the focus is on protecting the floor and I will only increase the fund's market exposure once the protection level has been surpassed – that is, once I am confident that at least 90% of the fund's value is protected in 12 months' time.

An example of this was the sharp decline in the FTSE/JSE All Share Index in May/June 2006. I decreased the fund's equity (share) exposure to less than 10% of total holdings, thereby protecting the floor. However, with the sudden upswing in the market from that point, the floor remained intact but the fund was unable to fully participate in this surge.

FT: How do you get the most out of a bull market?

Garth: I systematically increase exposure to shares, allowing the fund increased capture of positive returns. In a rising market, as the fund increases in value, the forward floor is adjusted upwards – securing gains already made and protecting them from future losses.

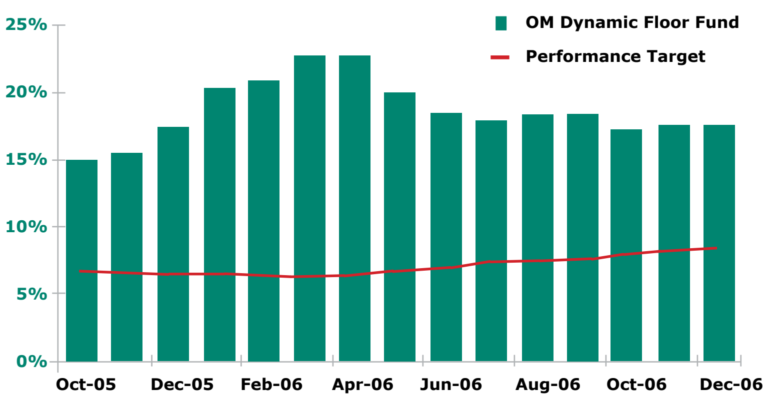
Since the Dynamic Floor Fund's inception in November 2002 to the end of December 2006, the highest return delivered over a 12-month rolling period has been 32% and the lowest 6%. The floor has been raised 51 times over this period. Interestingly, the fund's equity allocation has been as low as 5% and as high as 70% of the overall portfolio.

FT: Who should consider investing in this fund?

Garth: The fund is ideally suited to the more risk-averse investor who is concerned about losing money, but still wants to benefit from the growth potential of a share portfolio. It is also a suitable vehicle for retirement savings as it complies with section 28 of the Pension Funds Act.

* Figures sourced: S&P Fund Services, lump sum investment, distributions reinvested, charges excluded (unless stated otherwise).

Rolling 3-year returns on a monthly basis to end of December 2006



SERVICE SNIPPETS

Unit Trust Certificates invalid

Please note that these certificates are no longer valid. These have been cancelled and your account statement now provides you with proof of the units you own. If you are still in possession of a certificate, please destroy it.

Manage your portfolio online

To buy, sell or switch units online register on *My Secure Services* at www.oldmutualunittrusts.co.za.

Communicate via email

We have implemented a new communications system that allows you to receive your correspondence via email. The email option means you avoid postal delays and receive instant notification of completed transactions. Your annual account statements will continue to be posted to you, along with Financially Talking. Please call us at 0860 234 234 or email us at unittrusts@oldmutual.com if you would prefer to receive emails in future (they are in a PDF format and do not exceed 70 KB in size).

Drawing an income (Personal Living Annuity)

If you have an existing Old Mutual Personal Living Annuity, the product rules allow you to draw an annual income of between 5% and 20% of your investment value. This flexible feature of a living annuity introduces the risk that you could draw an income in excess of the growth of the investment. This would reduce the ability of the product to provide you with a sustainable flow of income over your lifetime. In the light of the current economic environment, it is prudent to consider the guidelines reflected below when deciding on a new annuity income level for the year ahead. These guidelines reflect the product rules of all new living annuities submitted to Old Mutual Unit Trusts.

Under age 70:	**Maximum 12% p.a.**
Between 70 and 80:	**Maximum 15% p.a.**
Over age 80/ill health*:	**Maximum 20% p.a.**

* If you are suffering from ill health or some other impairment that will significantly reduce your life expectancy.

It is all in the Outcome

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Investors have become increasingly risk averse – preferring products that protect against loss over and above those offering potentially high, long term growth.

Outcome-based funds attract investors nearing or in retirement who want to move from high growth focused investments to capital preservation or income-generating investments.

The appeal of outcome-based funds has been the amount of discretion given to the fund manager to pursue the fund’s objectives. These outcome-based funds typically invest across multiple asset classes (shares, bonds, listed property and cash) and tend not to have the constraints of the relative performance funds – where the mandate stipulates that they invest in a specific sector of the market, regardless of its performance. I again refer to my example of the Gold Fund. If gold shares fall in value, the fund has to continue investing its portfolio in gold and gold-related shares.

Outcome-based funds typically have a lower equity (share) allocation than, for example, a general equity fund. For this reason, these funds will generally not perform as well as an equity-only fund in a bull market. They are not designed to chase performance, but rather to deliver on a specific outcome.

Looking at Old Mutual Unit Trusts’ range of outcome-based funds (page 5), it becomes clear that even when their mandates may appear similar, the way in which they achieve these targets can be quite different. Investors need to be sure that they understand the mandate of the outcome-based fund in which they choose to invest. It is also advisable not to compare the performance of an outcome-based fund against funds in the peer group – as they all tend to have different mandates and investment objectives.

Your broker or licensed Old Mutual financial adviser can help you to select suitable outcome-based funds.

Old Mutual Unit Trusts' outcome-based funds

(refer to page 8 for fund performances)

Fund	Investment Universe	Client Need	Outcome (Performance Target)	Risk Target	Risk Rating (/5)#
Real Income Fund	▲ Money market ▲ Bonds ▲ Convertible bonds ▲ Preference shares ▲ Listed property (max 25%[1]) ▲ Shares (max 25%[1]) [1] a combined maximum of 35%	Investors needing a regular income stream with some capital growth – both increasing in line with inflation.	CPIX + 3% a year	Aims to avoid capital losses over rolling 18-month periods.	Moderately conservative (2)
Enhanced Income Fund	▲ Money market ▲ Bonds ▲ Inflation-linked bonds ▲ Securitised instruments ▲ Listed property (max 25%) ▲ Preference shares	Investors who require an income level higher than that produced by bank deposits and traditional income funds, but who can also accept a level of capital volatility in their investment.	BEASSA ALBI (1-3 year) Index – Total Return	Aims to have no negative returns over rolling 12-month periods.	Moderately conservative (2)
Dynamic Floor Fund	▲ Shares (max 70%) ▲ Property ▲ Bonds ▲ Money market ▲ Inflation-linked bonds ▲ Derivatives	Investors who want some capital preservation, but still want to participate in some market growth.	CPIX + 4% p.a. on rolling 36-month basis	Aims to protect 90% of net capital over rolling 12-month periods.	Moderate (3)
Galaxy Defensive Fund of Funds*	▲ Money market ▲ Bonds ▲ Inflation-linked bonds ▲ Listed property ▲ Shares	Investors seeking capital preservation but wanting access to some long term capital growth.	CPIX + 5% p.a. on rolling 36-month basis (gross of fees)	Aims to avoid capital losses over rolling 12-month periods.	Moderate (3)
Galaxy Balanced Fund of Funds*	▲ Money market ▲ Bonds ▲ Inflation-linked bonds ▲ Listed property ▲ Shares	Investors that are prepared to accept a moderate level of volatility in pursuit of long term capital growth and who have minimal short term income requirements.	CPIX + 7% p.a. on rolling 36-month basis (gross of fees)	Aims to avoid capital losses over rolling 18-month periods.	Moderate (3)
High Yield Opportunity Fund	▲ Shares (min 75%) ▲ Cash	Investors wanting a tax-efficient supplement to their income, coupled with potential for high, long term capital growth.	Dividend yield of not less than 5% on your net initial investment	None.	Moderately aggressive (4)

with 5 being aggressive and 1 being conservative

* Read more about these funds on page 6.

A Galaxy of choice for you

Old Mutual Unit Trusts now offers you access to multi-manager funds. Our previous range of unit trusts were all managed by Old Mutual's in-house fund managers. The Galaxy multi-manager funds, on the other hand, appoint a number of fund managers from different investment houses to manage portions of each fund.

Although the Galaxy funds have been available via Investment Horizons, Max Investments and Fairbairn Capital, it's the first time they can be accessed directly from the Unit Trust division. These funds are managed by SYmmETRY Multi-Manager, a specialised investment business within Old Mutual. SYmmETRY administers the funds and appoints appropriate fund managers – researching and monitoring talented fund managers across the country. Their manager selection process is aimed at finding skilful managers who will consistently deliver performance without exposing investors' money to undue risk. SYmmETRY portfolios have won several awards for top risk-adjusted returns.

The following funds are available via Old Mutual Unit Trusts:

Galaxy Equity Fund of Funds hold underlying funds which invest across all sectors of the FTSE/JSE All Share Index, with the aim of outperforming its peer group average (Domestic-Equity-General) over the long term. The fund is suitable for investors who are prepared to accept a high level of volatility in pursuit of high, long term capital growth.

Galaxy Balanced Fund of Funds offers a balance between capital growth and capital protection. It seeks to grow capital significantly in excess of inflation (CPIX + 7% p.a. over rolling 3-year periods). In addition, it aims to avoid capital losses over any 18-month period. To achieve these investment objectives, the underlying fund managers have the freedom to select from a range of assets, namely money market instruments, bonds, inflation-linked bonds, listed property and shares. The fund is suited to those investors seeking capital growth at lower levels of volatility than a fund fully invested in shares.

Galaxy Defensive Fund of Funds aims to avoid capital losses over any 12-month period and offers some level of growth (CPIX + 5% p.a. over rolling 36-month periods). The fund is suitable for the more risk averse investor seeking some capital growth at relatively low levels of volatility. To achieve this, the underlying fund managers invest across money market instruments, bonds, inflation-linked bonds, listed property and shares.

Galaxy Fixed Interest Fund of Funds has a strong bias toward capital preservation. It is aimed at investors seeking high levels of income with a possibility of some capital growth over the long term. Income is derived from a range of interest-bearing assets, including some exposure to listed property shares. The fund aims to outperform the BEASSA All Bond (1-3 year) Index.

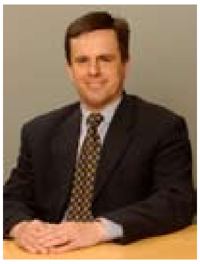
	Performance			Positive months (/66m)*	Risk Rating (/5)	Investment Minimums	
Funds	1 year	3 years (p.a.)	5 years (p.a.)			Lump Sum	Monthly
Galaxy Equity	36%	35%	22%	41/66	4	R10 000	R500
Galaxy Balanced	24%	26%	22%	47/66	3	R10 000	R500
Galaxy Defensive	17%	21%	19%	53/66	2	R10 000	R500
Galaxy Fixed Interest	8%	9%	10%	60/66	2	R15 000	R1 000

* Positive months refer to the number of months that the funds delivered positive returns. All funds were launched on 1 June 2001. Figures sourced from S&P Fund Services to end December 2006, based on lump sum investments with distributions reinvested and charges excluded.

To find out more about these funds speak to your broker or Old Mutual financial adviser. Alternatively you can call 0860 234 234 or visit www.oldmutualunittrusts.co.za.

Know what it really costs you (TER explained)

Chris Potgieter, Financial Director, Old Mutual Unit Trusts



The unit trust industry is introducing a new measure to evaluate the effect of costs on your investments. This measure is called a Total Expense Ratio (TER).

Total expense ratios are used globally to measure the impact of management and operating costs deducted from a fund's portfolio.

Although you know what your initial charge is before you invest, it is not possible to quantify all of the portfolio charges upfront. These costs generally include the annual service fee, performance fees, the fund's bank charges, levies and taxes (e.g. UST), custodian and trustee fees, stockbroker fees and the audit fees. These are deducted from the portfolio's income on a monthly basis. Of these charges, only annual service fees are disclosed upfront in the fund fact sheet.

Investors generally incur charges in the following ways:

Maximum upfront charges disclosed on fund fact sheet.	One-off initial charge deducted from a new investment before units are bought (it comprises an administration fee and commission for advice).
Annual fee agreed upfront between adviser and client.	Ongoing adviser fees deducted through the sale of units.
Range of charges individually disclosed in annual report.	Ongoing management and operating costs deducted from the fund's portfolio.

The TER of a fund gives you an indication of how these costs affect your returns. Expressed as a percentage, a fund's TER is calculated by dividing its total portfolio costs by its total assets. The fund's total assets are the daily average value of the portfolio over a specific period (e.g. a financial year).

As per the ACI* requirements, all funds' TERs must be published in the fund fact sheets from April 2007 onwards – with the exception of funds of funds, which must be published from July onwards.

$$\text{Total Expense Ratio} = \frac{\text{Total Costs}}{\text{Total Assets}}$$

The benefit of a TER is that it enables you to compare differently structured investments, e.g. costs related to investing in funds of funds versus investing in single manager funds. Bear in mind, though, that the TER is calculated using historical information and it may not necessarily be an indication of future expenses.

The **FUND FACT SHEETS** are updated after each calendar quarter-end. They contain fund details, charges, updated performance figures and comments from the fund managers. Fact sheets are available from your financial adviser, our Service Centre (0860 234 234) or our website www.oldmutualunittrusts.co.za.

"It is important that investors realise that costs are just one of a number of factors to consider when choosing or assessing a portfolio's prospects," says Di Turpin, ACI Chief Executive. "The value of TER is that it allows you to track your portfolio's expenses and also to directly compare various financial services products. We hope that other products will adopt this measure as well, resulting in far better disclosure for the consumer. The collective investments industry has always offered low cost investments and been transparent, giving investors full information on costs and performance. We see TERs as another strategic tool for the investor."

ACI

* The **Association of Collective Investments (ACI)** represents the interests of South African unit trust management companies and their investors. Membership of management companies is voluntary and, together with the ACI, they work on the principles of self-regulation. The primary aim of the Association and its members is to facilitate the development and growth of the industry, through its dealings with the authorities and regular communication with the media and investing public.

Investment team under new name

In August 2006, Old Mutual Asset Managers announced its decision to move to a boutique structure. The new investment business is made up of 12 separate investment boutiques. These boutiques consist of small teams, focused on a particular area of investment expertise. Each team has the freedom to make their own investment decisions and the remuneration of the team is directly related to the performance they deliver. The boutiques form part of the new **Old Mutual Investment Group** (a name that now replaces Old Mutual Asset Managers).

Fee changes for offshore funds

The International Growth Fund of Funds and Global Bond Feeder Fund changed their initial charges on 1 January 2007. The reason for the change is to standardise charges across all our funds. The initial charge is deducted from all new investments (including regular debit orders) and comprises an administration fee and commission for advice (maximum 3%, negotiable).

Standardising the administrative fee means that:

- For investments of R5 000 and more, per fund, no administration fee is charged (only commission).
- For investments below R5 000:
  - Our equity funds charge a maximum 2% administration fee (excluding VAT). International Growth Fund of Funds has increased its administration fee from 1% to 2% (maximum initial charge is 5.74% including commission and VAT).
  - Our income and bond funds charge a maximum 0.4% administration fee (excluding VAT). Global Bond Feeder Fund has reduced its administration fee from 1.4% to 0.4% (maximum initial charge is 1.14% including commission and VAT).

	Performance % p.a.		
FUND	**1 year**	**3 years**	**5 years**
Balanced Fund	31.0	29.5	19.5
Dynamic Floor Fund	10.3	17.4	n/a
Enhanced Income Fund	8.6	n/a	n/a
Financial & Industrial Fund*	35.5	37.6	25.6
Financial Services Fund	36.1	41.6	24.9
Flexible Fund	32.1	32.8	22.1
Four Plus Capital Fund of Funds	7.9	12.4	n/a
Four Plus Global Fund of Funds	25.4	21.2	10.7
Four Plus Growth Fund of Funds	22.6	25.9	19.1
Four Plus Secure Fund of Funds	5.4	6.3	n/a
Galaxy Balanced Fund of Funds	24.2	26.4	21.8
Galaxy Defensive Fund of Funds	17.1	20.7	19.2
Galaxy Equity Fund of Funds	36.1	34.9	22.2
Galaxy Fixed Interest Fund of Funds	8.3	9.0	10.3
Gilt Fund	4.7	10.2	12.7
Global Bond Feeder Fund	18.3	5.3	-1.4
Global Equity Fund A	37.0	19.6	2.3
Global Technology Fund	20.0	7.2	-9.7
Gold Fund	27.5	15.4	20.7
Growth Fund	37.0	39.0	29.0
High Yield Opportunity Fund	33.8	39.4	33.7
Income Fund	6.4	8.2	9.8
Industrial Fund	31.7	38.5	32.5
International Growth Fund of Funds	28.5	13.8	-1.6
Investors' Fund	35.1	37.1	25.7
Mining & Resources Fund	49.9	39.9	29.8
Money Market Fund	7.2	7.2	9.0
SA Quoted Property Fund	23.0	35.1	n/a
Small Companies Fund	41.4	44.6	34.7
Top 40 Fund	38.1	34.9	19.6
Top Companies Fund	33.0	36.0	26.5
UK Money Market Feeder Fund	28.2	7.6	-1.6
Value Fund	34.4	38.4	29.0
South Africa CPI	**6.0**	**4.3**	**5.1**

Source: Standard & Poor's Fund Services. Lump sum investments to the end of December 2006, distributions reinvested and NAV-NAV prices used (i.e. initial charges excluded). Old Mutual Unit Trusts has been licensed by the JSE Securities Exchange SA to use the FTSE/JSE Top 40 Index name.

* Note: Old Mutual Financial & Industrial Fund has merged to become Old Mutual Industrial Fund R.