FOREWORD

DID YOU KNOW? BERNANKE PUT

The term *Bernanke Put* derives from the Greenspan Put, which was coined to describe US Federal Reserve Chairman Alan Greenspan's 1988 response to the collapse of hedge fund manager, Long-Term Capital Management L.P. Greenspan quickly lowered interest rates, which encouraged investors to borrow money cheaply to prop up share and bond markets. Ben Bernanke succeeded Alan Greenspan in 2006 and was Fed Chair during the global financial crisis.

A put option allows an investor to sell an investment to a counterparty when its price declines to or below the option's strike price. Investors began to expect sharply lower US federal funds rates to come to the rescue for any major market shock. In effect, the US Federal Reserve created an artificial put option or price floor in the order of 20% below prevailing market prices.

While there is no formal guarantee, the practice has drawn criticism for the moral hazard of encouraging excessive risk taking, socialising stock market losses and privatising stock market profits.

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IN THIS ISSUE

FIRST QUARTER IN REVIEW

The first quarter of 2018 turned out to be eventful after global share markets suffered a sizable correction and South Africans experienced meaningful political change. NICK CURTIN puts these developments into context.

After a major bull run, global share markets suffered their first negative months since 2016 and the largest correction in over two years. Developed market bond yields have moved up decisively, with the US 10-year Treasury yield flirting with the 3.0% level. Synchronised economic growth, emerging inflation and an increasingly hawkish US Federal Reserve all point to rising volatility.

The resignation of President Jacob Zuma and election of President Cyril Ramaphosa dominated South African news. The cabinet reshuffle was pleasing, albeit with some degree of expected political compromise. The key economic cluster portfolios have been handed to well–regarded, competent ministers.

But while global markets face the challenges of rising interest rates and rising inflation — brought about by faster economic activity and full employment — South African economic growth is lacklustre, with disinflationary consequences. The unemployment rate is high and investment spend low, brought about by weak domestic savings.

South Africa therefore relies on excess foreign investor savings to fund the external deficit, which is likely to weaken from the current 2% of GDP. Government's fiscal deficit has concurrently worsened to almost 5% of GDP due to low tax collection, rising corruption losses, SOE mismanagement and real growth in government consumption and interest expenditure.

The budget contained several policy proposals to increase revenue collection. These included the 1% VAT rate increase, bracket creep and increased quasi-taxes like the fuel levy. These policy responses are significant headwinds to consumption-led economic growth. Government has also diverted much-needed funding from infrastructure investment to free tertiary education and real social grant increases. These are growth-negative policy responses.

However, nascent household and business sentiment should not be underestimated. Already, the rand–dollar exchange rate is back to early 2015 levels and share prices of JSE-listed 'SA Inc.' companies have surged. Yet retailers continue to warn of relatively poor trading prospects, due to low volume growth, low-to-negative price inflation and currency headwinds to the translation of earnings from offshore businesses bought in the last five years.

Over paying for an investment that fails to deliver the required earnings growth is one of the biggest contributors to permanent capital losses. We should therefore remove sentiment and emotion from facts and reality. Falling discretionary spending power means the SA consumer is facing a very tough period ahead and investment in SA retailers at current prices is not wise.

Although valuations are full, we still believe global equity markets will be supported by a generally–positive corporate earnings environment. **Foord's defensive investment strategy in these conditions favours global equities within the parameters of the investment mandates, avoids expensive 'SA Inc.' shares and seeks to lock-in high, fixed yields on SA cash and bond instruments given prospects of benign SA inflation.**

Despite a poor relative performance period over the previous 12 to 18 months, the Foord portfolios are extremely well positioned for the unfolding environment. Our investment thesis that the coming decade will look very different to the previous is playing out as we move deeper into the multi-decade inflection point in capital markets.

FOORD FLEXIBLE FUND **TURNS TEN**

On 1 April 2018, the Foord Flexible Fund of Funds celebrated its tenth anniversary. We summarise DAVE FOORD's recent presentation on the fund's objective and achievements.

Foord has managed long-term asset allocation strategies since the early 1980s, mostly constrained by the asset allocation limits prescribed by Regulation 28 of the Pension Funds Act. The primary constraints being international assets (limit of 30%) and asset class exposures (maximum 75% in equities, for example).

Judicious diversification truly is the only free lunch in investing and our view is that the Regulation 28 limits are arbitrary and nonsensical. If anything, they are counter-productive to creating optimal risk/return portfolios for long-term South African investors.

Exchange controls were first relaxed in the late 1990s, giving South African investors gradual access to global investment markets (pension funds could initially only invest 15% of their portfolios abroad). At the time, the JSE comprised over 700 companies. This has declined to 300 counters today, only 90 of them practically investable (having a market capitalisation of more than R10 billion). This decimation of the investment opportunity set was accompanied by consolidation within industries too, further narrowing investment choice in South Africa.

It was against this background that the Foord Flexible Fund of Funds was established in 2008. We felt that a well-managed portfolio not constrained by Regulation 28 would be better placed to achieve consistent, inflation-beating returns over the long term. In short, we believe we built a better mousetrap.

We expected (and maintain this view today) that the Foord Flexible Fund should outperform the Foord Balanced Fund by around 2-3% per annum over a full investment cycle. We also believed that, where possible, converting compulsory savings from Foord Balanced Fund to Foord Flexible Fund would accordingly lead to superior risk/return outcomes over time, notwithstanding the once-off tax charge that would eventually need to be paid anyway.

As we reach the Foord Flexible Fund's tenth birthday, it is with some pride that we reflect on a very successful first decade for investors in Foord's flagship, best investment view portfolio.

> THE FOORD FLEXIBLE FUND SHOULD OUTPERFORM THE FOORD BALANCED FUND BY AROUND 2-3% PER ANNUM OVER A FULL INVESTMENT CYCLE.

BEST INVESTMENT VIEW

Since inception, the inflation plus 5% investment objective has been comfortably exceeded. This growth is more pleasing given the weak markets during the global financial crisis of 2008/9 (the first two years of the fund's existence). The Foord Flexible Fund has outperformed the Foord Balanced Fund by 2.3% per annum (both after fees) for ten years, almost precisely in line with expectation and the key rationale for launching the fund.

This excess return has been achieved despite the short-term rand strength of the last eighteen months and the fund having a much higher weighting to foreign assets than the Foord Balanced Fund. The international assets have grown more in US dollar terms than the rand has strengthened against the dollar. This vindicates our decision to maintain the largest exposure to our preferred global equity ideas, where investment choice is vast.

DYNAMIC ASSET ALLOCATION

The fund's dynamic asset allocation ability is its key differentiator. The unique combination of asset allocation and security selection capabilities has always been Foord's core competitive strength. The Foord Flexible Fund allows us to exploit these opportunities. Whereas the global investment component of the Foord Flexible Fund has gone from 15% in 2008 to 70% currently, the Foord Balanced Fund has until recently been limited by the 25% foreign assets limit (the limit was increased to 30% in February 2018).

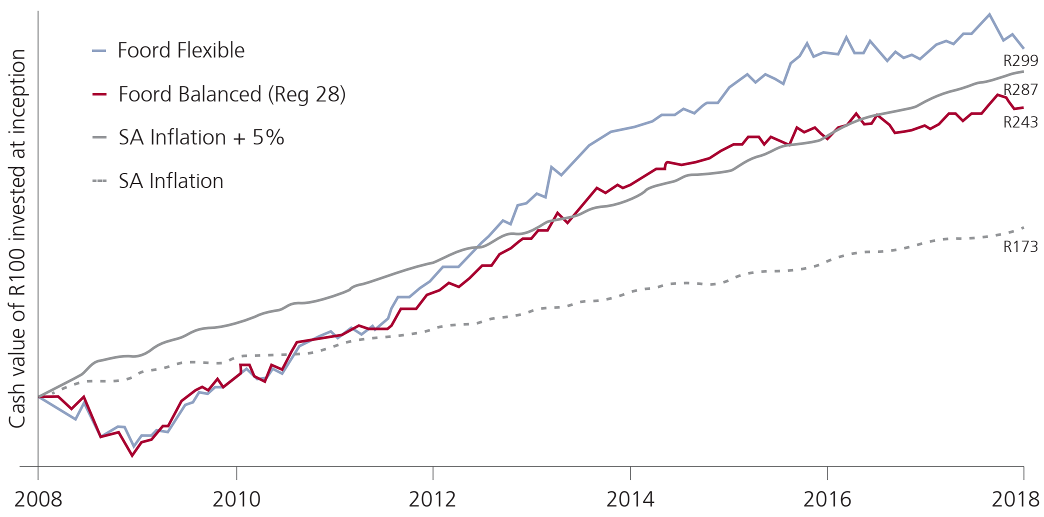
The Foord Flexible Fund's ability to implement Foord's best investment view unhindered has been key to its superior risk/return outcomes. We expect this pattern to continue.

The high foreign asset weighting in the portfolio stands out. In our view, the choice, diversification and valuation of global equities means they are Foord's preferred asset class to meet or exceed the fund's investment objective in the long term. The Foord International Fund and the Foord Global Equity Fund are populated with high-quality businesses operating in industries and geographies not available locally, with attractive above-average earnings growth prospects over the coming years.

Recent rand strength will eventually turn, providing a meaningful additional tailwind to performance as the cycle plays out. The vastly different asset allocation today compared to ten years ago is testament to Foord's forward-looking investment philosophy and illustrates our view that the next decade will look very different to the last.

The Foord Flexible Fund is our flagship, best investment view portfolio for investors seeking inflation-beating returns for discretionary savings.

FOORD FLEXIBLE FUND CUMULATIVE RETURNS (CLASS R)



PROTECTING AGAINST RISK OF LOSS IN THE LATE STAGES OF A BULL MARKET

We've written before how business cycles drive market cycles. WILLIAM FRASER explains why Foord underperforms during the late stages of a bull market.

Since the 2009 global financial crisis market lows, share investors worldwide have benefited from the aftereffects of the Bernanke Put (see *Did You Know?*). Massive American, European, British and Japanese central bank stimulus found its way into markets, lowering volatility and boosting share and bond prices.

Central banks also lowered interest rates to near or below zero percent. Negative real rates forced savers to seek capital growth elsewhere. Share and high-yielding corporate debt markets became the default asset class for investors.

Consequently, real earnings' yields fell over the now almost nine-year bull market as prices rose. Market valuations, measured by price-earnings ratios, surged above their long-term means. Sectors geared to faster economic growth experienced outsized gains and companies exposed to the knowledge economy ballooned. Old economy stocks, with more predictable, but slower, earnings growth, lagged.

But it wasn't all about prices. As the economic cycle progressed, lower interest rates and steady employment gains augmented company earnings. As sentiment and consumer demand recovered, manufacturers boosted output, increasing demand for commodities. Soon, capacity became constrained and companies borrowed cheaply to build more factories or invest in new machines. Wages finally rose as skill shortages became endemic. Investor confidence improved and more capital became available for business and stock markets.

The economic cycle found a natural rhythm not unlike those that came before. It is typical for share prices to lag the cycle in the early stages when investor sentiment is low. This provides a good entry point for long-term investors. But it is also common for excessive share market exuberance at the end of the cycle, particularly as investors chase returns in specific sectors or themes.

In our view, we are slowly nearing the end of the second-longest economic expansion in living memory. But despite the rich valuations, markets may continue to advance as investors extrapolate favourable conditions, increasing the risk of permanent capital loss.

Given current valuations, global share market returns should be muted over the next five years (on some metrics, the US S&P500 Index is the third most expensive in its 120-year history). The bull market in developed market bonds is already over. In South Africa, macro-economic headwinds imply great difficulty for 'SA Inc.' companies to grow earnings meaningfully.

Foord's South African portfolios are accordingly conservatively structured. Share weightings within portfolios are below long-term averages, while SA bond and cash holdings are higher. Within equities, we have avoided companies on very expensive market multiples in preference for companies with more stable earnings' prospects and much lower risk of loss.

This investment strategy will underperform in the late stages of an economic cycle when investor exuberance is highest. Long-term Foord investors will recognise the current relative underperformance patterns and approve the strategy.

The calendar year returns of Foord's equity portfolios provide evidence of its success: the FTSE/JSE All Share Index has suffered seven negative calendar years since 1984, while Foord investors have braved just two.

BENCHMARK CHANGES

There are two upcoming benchmark and fee changes that affect investors in the Foord Equity Fund and Foord Flexible Fund of Funds. The changes will become effective on 1 July 2018. DIANE BEHR provides the details.

FOORD EQUITY FUND

The performance measurement benchmark of the Foord Equity Fund will change from the FTSE/JSE All Share Index (ALSI) to the FTSE/JSE All Share Capped Index (CAPI). This change will affect the calculation of performance fees for all performance fee unit classes.

While Foord historically regarded the ALSI to be the most representative SA equity market index, the ALSI has become very concentrated. The top five shares amount to 40% of its market capitalisation and the top ten shares amount to 55%. At 31 December 2017, the largest share in the ALSI, Naspers N, accounted for almost 20% of the ALSI market cap (31 December 2016: 13.6%, 2015: 12.9%).

The CAPI follows the construction of the ALSI with regards to constituents, data and application of corporate actions, but caps the index constituents at a fixed level of 10%. Both indices are market capitalisation weighted and subject to free float rules and include almost all companies listed on the JSE mainboard irrespective of their shareholder weighting (companies with a minimal free float are excluded).

The change will affect future benchmark performance reporting and the accrual of performance fees for all performance fee unit classes. There will be no change to Foord Equity Fund's investment strategy or portfolio construction.

FOORD FLEXIBLE FUND OF FUNDS

The performance fee measurement methodology of the Foord Flexible Fund of Funds will change from an effective one-day methodology to a rolling 365-day

methodology. The purpose of the change is to align the methodology with that used on the Foord Balanced, Foord Equity and Foord Conservative Funds.

The new methodology applies the performance sharing rate, for example 10%, to the fund's one-year performance variance each working day, accruing a performance fee (alternatively the minimum fee) for the number of days since the previous accrual. All things being equal, fees for outperformance are earned only over a full year, while underperformance results in a lower-than-benchmark or minimum fee, for a full year. This methodology smooths out the performance measurement period and avoids large, but short-lived, performance variances from meaningfully affecting fee accruals.

The change will affect only the performance fee calculation methodology for all performance fee unit classes. The fund's benchmark remains inflation plus 5% per annum. There will be no change to Foord Flexible Fund of Fund's investment strategy or portfolio construction.

MARKETS IN A NUTSHELL

WORLD

EQUITIES

Despite expectations for increased corporate earnings, global equity markets fell as the US-China trade spat intensified – and tech stocks retraced some of their outsized 2017 gains on user data privacy concerns

BONDS

Developed market bond yields initially advanced meaningfully on expectations of a more hawkish Fed policy stance – but moderated latterly

CURRENCIES

The US dollar weakened against other majors – the Fed forecast for three 2018 interest rate increases was unchanged against market expectation of potentially four

COMMODITIES

Global commodity prices were mixed with iron ore and copper weakening as investors contemplated the US-China trade war implications – but oil rose as OPEC producers and partners appear set to comply with production limits

ECONOMY

Developed market economies continued to expand above sustainable long-term growth rates but inflation was contained – wage increases were surprisingly subdued despite falling unemployment rates

MONETARY AND FISCAL POLICY

New Federal Reserve Chairman Powell announced a further 0.25% increase in the federal funds target rate, taking it to 1.75% – the "dot plot" continues to indicate a gradual path of rate increases into 2019

SOUTH AFRICA

EQUITIES

The FTSE/JSE All Share Index (-6.0%) tracked global share markets lower – index heavyweight Naspers declined 16% and the Resilient property stable prices more than halved on ongoing corporate governance concerns

BONDS

Moody's confirmed SA's local currency rating at BBB- while improving the outlook from negative to stable – bond yields continued to firm during the quarter propelling the All Bond Index (+8.1%) higher

CURRENCIES

Cyril Ramaphosa was sworn in as South Africa's president after Jacob Zuma reluctantly resigned – the rand strengthened further on sentiment and foreign portfolio inflows

ECONOMY

Q4 2017 GDP growth surprised positively after household consumption advanced more than anticipated – but the current account deficit widened as increased income payments to foreigners offset terms of trade gains

MONETARY AND FISCAL POLICY

The SA Reserve Bank lowered the REPO rate by 25 basis points to 6.5% – given the benign inflation environment and stronger rand

FUND OBJECTIVE

FOORD FLEXIBLE FUND OF FUNDS

ZA

Inception date: 1 April 2008

The fund seeks to provide investors with a net-of-fee return of 5% per annum above the annual change in the South African Consumer Price Index, measured over rolling three year periods. It aims to achieve this objective by exploiting the benefits of global diversification in a portfolio that continually reflects Foord Asset Management's prevailing view on all available asset classes, both in South Africa and abroad.

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	11.6	2.9	-2.9	-5.7
Benchmark	11.1	11.0	9.3	2.2

Benchmark: CPI + 5% per annum, which is applied daily by using the most recently available inflation data and accordingly will be lagged on average by 5 to 6 weeks.

FOORD BALANCED FUND

ZA

Inception date: 1 September 2002

The fund aims to achieve the steady growth of income and capital as well as the preservation of real capital (capital is adjusted for inflation). The portfolio is managed to comply with the statutory investment limits set for retirement funds in South Africa (Regulation 28).

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	14.1	2.2	0.5	-3.8
Benchmark	12.6	4.6	5.1	-3.2

Benchmark: The market value weighted average total return of the South African Multi Asset High Equity unit trust sector, excluding Foord Balanced Fund.

FOORD CONSERVATIVE FUND

ZA

Inception date: 2 January 2014

The fund aims to provide investors with a net-of-fee return of 4% per annum above the annual change in the South African Consumer Price Index, measured over rolling three-year periods. The portfolio is managed to comply with the statutory investment limits set for retirement funds in South Africa (Regulation 28).

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	5.4	3.6	2.7	-2.2
Benchmark	9.6	9.9	8.4	2.1

Benchmark: CPI + 4% per annum, which is applied daily by using the most recently available inflation data and accordingly will be lagged on average by 5 to 6 weeks.

FOORD EQUITY FUND

ZA

Inception date: 1 September 2002

The fund aims to earn a higher total rate of return than that of the South African equity market, as represented by the return of the FTSE/JSE All Share Index including income, without assuming greater risk.

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	16.3	-1.6	-4.6	-7.2
Benchmark	15.2	5.0	9.6	-6.0

Benchmark: Total return of the FTSE/JSE All Share Index

FOORD INTERNATIONAL FUND

LUX

USD

Inception date: 1 August 2014

The fund aims to achieve meaningful inflation-beating US$ returns over rolling five-year periods from a conservatively managed portfolio of global equities, warrants, exchange traded funds, UCITS and other UCIs, interest bearing securities and cash instruments reflecting Foord's prevailing best investment view.

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	6.7	4.1	5.7	-3.6
Benchmark	2.1	1.9	2.4	0.7

Benchmark: US inflation

FOORD GLOBAL EQUITY FUND

SG

USD

Inception date: 1 June 2012

The fund aims to achieve optimum risk adjusted total return by investing primarily in a diversified portfolio of global equities. Without assuming greater risk, it seeks to achieve a higher total rate of return than the MSCI All Country World Net Total Return Index.

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord**	8.1	6.5	14.5	-2.5
Benchmark	11.7	8.1	14.8	-1.0

Benchmark: MSCI All Country World Equity Index.

NOTE: Investment returns for periods greater than one year are annualised | * Class R, Net of fees and expenses | ** Class B, Net of fees and expenses

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