momentum

# Smooth Bonus Report

Fourth Quarter 2015

*With us the safest distance between two points is also the smoothest*

*Dear valued investors*

## Recapping the 4th quarter of 2015

The final quarter of 2015 pronounced the end of almost a decade without interest rate increases in the US. The US Federal Reserve raised interest rates by 0.25% in December 2015 on the back of stronger US data (firm economic growth prospects, tightening labour market and continued strength in the housing market). Investor sentiment towards South Africa became increasingly bearish over the quarter due to the finance minister reshuffle, weaker commodity prices, a slowing economy and the Fitch Rating's downgrade to just one notch above junk status. The Rand weakened by more than 25% for the year.

In the 4th quarter of 2015, the JSE/FTSE All Share Index was up by 1.7%. Industrials was the best performing sector with a gain of 6.6% vs losses of 3.3% for Financials and 19.2% for Resources. The JSE All Bond Index weakened by 6.4%, dragging the FTSE/JSE SA Listed Property Index down by 4.7%. On the global front the MSCI World Index returned a positive 5.6% in USD.

Herman van Papendorp and Sanisha Packirisamy from Momentum Investments provide further market and economic commentary on page 9, as well as their inflation expectations for 2016 on page 4.

Despite the increase in equity volatility, and below inflation returns from South African equities and bonds for 2015, all our smooth bonus portfolios have outperformed their respective benchmarks.

## Allocation to Africa ex-SA Real Estate, Multi-Manager Smooth Growth Fund Global and Multi-Manager Secure Growth Funds

Regulation 28 of the Pension Funds Act allows for an additional 5% investment in Africa. An initial investment of 2.5% was made via an Africa ex-South Africa listed equity fund with Coronation in March 2015. Effective November 2015 the strategic asset allocation was adjusted upwards by 0.1875% to allow for an initial investment into an Africa ex-SA Real Estate development fund managed by Momentum Global Investment Management. This allocation will increase to 2.5% over time as requests for funding are made for development projects.

Strategic asset allocation modelling for both Africa ex-SA real estate and listed equity at 2.5% showed an improved risk-adjusted return. The Africa ex-SA real estate funds leases are primary in USD, or linked to USD, which slightly mitigates currency risk. This, together with a combination of strong economic growth, young demographics, a growing middle class and plentiful resources, makes the Africa frontier market a compelling investment.

David Lashbrook from Momentum Global Investment Management gives further insight for investing in commercial real estate in frontier Africa on page 7.

Wishing you many happy returns

**Warm regards**

*Willem Gaymans*
Investments Product Specialists: Corporate Clients
MMI Corporate and Public Sector

# Contents

# Inflation expected to head higher over 2016

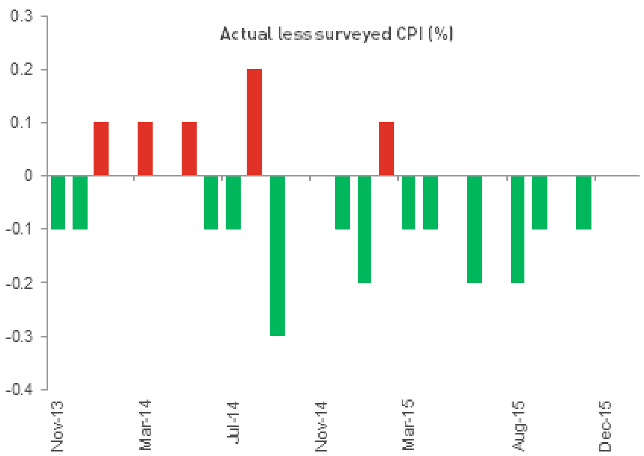
By Herman van Papendorp and Sanisha Packirisamy

**Headline inflation averaged 4.6% y/y in 2015, but inflation is expected to breach the target on average in 2016.**

According to Stats SA, headline consumer price inflation (CPI) rose to 5.2% y/y in December 2015 from 4.8% y/y in November, in line with market estimates. This leaves average headline inflation for the full year (2015) at 4.6% y/y.

The direction of inflation has largely been to the downside for the most part of 2014 and 2015 (see chart 1), i.e. surprising positively, but an increasingly volatile and weaker trade-weighted currency, extreme drought conditions and administered price pressures are likely to drive the headline print higher over the course of 2016.

**Chart 1: Positive CPI surprises have been a common trend over 2014 - 2015**



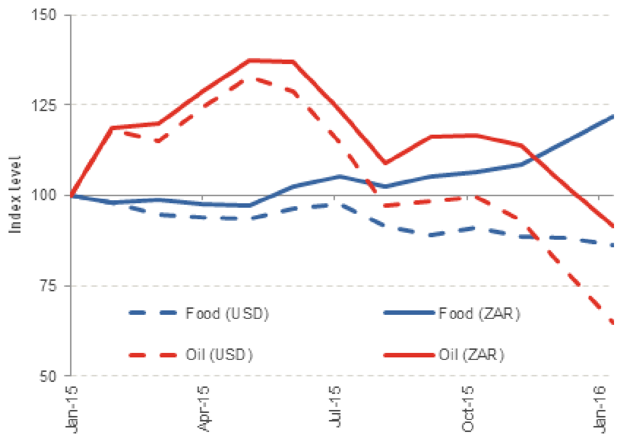

*Source: Stats SA, Bloomberg, Momentum Investments*

December represents a high survey month, with over 37% of the basket being surveyed in addition to the normal monthly surveys. This led to a 0.3% rise in the headline inflation print in month-on-month terms. Relative to our own forecasts, personal care costs and clothing prices surprised to the upside, while the escalation in food prices continued to surprise to the downside.

## Prolonged drought conditions and rand weakness to lead food inflation higher over upcoming months

Food inflation rose by a lower than expected 0.6% m/m in December, leaving the year-on-year rate just marginally below the upper 6% target at 5.9%. A strong El Nino weather pattern has led to the worst drought conditions in decades for South Africa, severely affecting our ability to plant maize. According to the Bureau for Food and Agricultural Policy, SA's total maize crop is expected at 4.7 million tonnes, significantly lower than the country's average consumption of 9.6 million tonnes per year. This will likely result in SA importing agricultural commodities such as maize and sugar, forcing food prices higher in 2016. A steep depreciation in the currency places further upward pressure on food inflation. Despite healthy global stock levels of rice, wheat and maize, which have left dollar-based food prices nearly 10% lower than they were a year ago, in rand terms, food prices are considerably higher.

**Chart 2: Weaker rand negating positive impact of lower international food prices**




*Source: Stats SA, Global Insight, Momentum Investments*

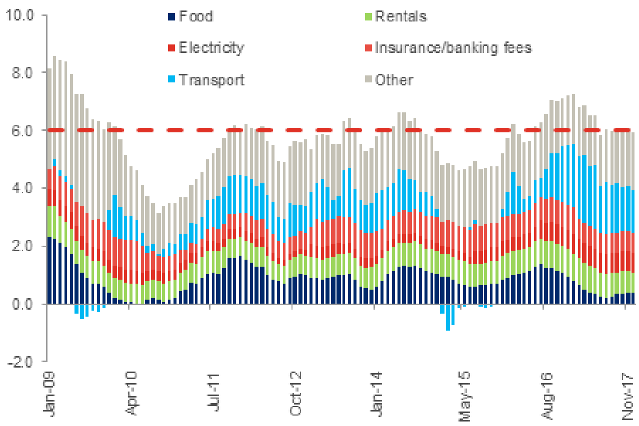
In addition to low international food prices, margin compression and low transport costs could help to contain food price pressures in 2016 at the margin. As such we anticipate a rise in food inflation from 5.1% on average in

2015 to close to 8% in 2016.

### Marginally lower petrol prices in January, but under-recovery points to a hike in February

Petrol prices were hiked by a negligible 1c/l in December, while lower oil prices outweighed currency weakness in January leading to a 3c/l cut in petrol prices. Nevertheless, the current under-recovery points to a 9c/l hike in February based on recent rand movements relative to the change in international oil prices. We expect further rand weakness and a gradual increase in oil prices to play a larger role in boosting inflation prints over the course of 2017 via the transport component (see chart 3).

**Chart 3: Contribution to actual and forecasted headline inflation (% y/y)**




*Source: Stats SA, Global Insight, Momentum Investments*

### Jump in administered price inflation

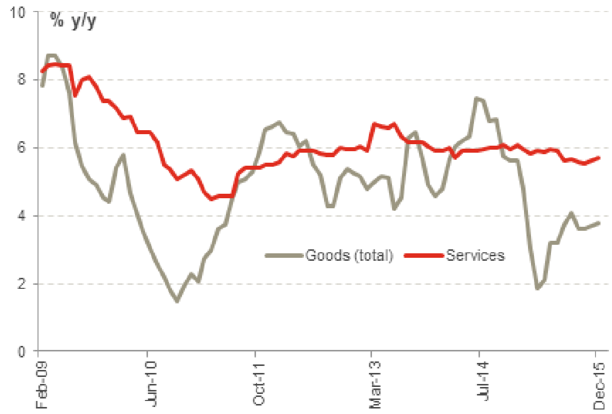
Administered price inflation shot up from 3.9% y/y in November to 5.8% y/y in December 2015, but remained well below the longer-term average of 7.3% y/y since 2009. We expect a further ramp up in administered price inflation later this year on the back of further steep increases in the electricity tariff. Eskom has applied for a R22.8 billion adjustment for its 2013/14 financial year which could lead to an electricity tariff increase of close to 17%.

### Core inflation rises, while services inflation remains sticky at elevated levels

Core inflation (headline ex-food, non-alcoholic beverages and petrol) ticked higher from 5.5% to 5.6% y/y in December 2015, but showed few signs of a more aggressive currency pass-through despite a 24% weakening in the currency on a trade-weighted basis since the beginning of 2015.

Services inflation tracked sideways at 5.7% y/y in December (see chart 4), printing a tad lower than the 6.0% average experienced since 2012. Meanwhile goods inflation shifted above the mid-point of the 3% - 6% inflation band for the first time in a year from 3.8% y/y in November to 4.6% y/y in December 2015. This was largely due to non-durables (food) inflation picking up to 5.3% y/y in December from 4.0% y/y the month before, whereas durables (furniture and appliances) inflation remained at the lower end of the target and semi-durables (clothing) inflation slowed to 3.4% y/y over the corresponding period.

**Chart 4: Sticky services inflation**




*Source: Global Insight, Momentum Investments*

### Expected breach of the target and deterioration in inflation expectations to drive interest rates higher

In our view, inflation risks are firmly tilted to the upside. Ongoing currency weakness (and volatility), prolonged drought conditions leading to higher food inflation and an anticipated steep rise in electricity tariffs are likely to drive a further acceleration in inflation from the 4.6% y/y average print in 2015 to an estimated average rate of 6.4% this year, potentially peaking above 7% in 4Q16. We expect inflationary pressures to persist in 2017, estimating a 6.3% y/y rise on average.

Moreover the inflation expectations of the price-makers in the economy, namely businesses and trade unions, have deteriorated sharply over the past year. According to the inflation survey results from the Bureau of Economic Research, SA firms are expecting headline inflation to average 6.5% y/y over the next five-year period, while trade unions see inflation averaging 6.2% y/y over the same time period. These expectations have increased from 6.1% and 6.0% y/y, respectively, a year ago.

Although a weaker currency could promote higher export growth, currency volatility, infrastructure bottlenecks and higher imported input costs are likely to dampen SA's export elasticity to a weaker trade-weighted rand. Similarly, lower rand-sensitive imports could be partly offset by higher agricultural imports which could leave the current account deficit relatively extended over 2016. The outlook for net foreign inflows is likely to deteriorate in an environment where firmer growth in the United States (US) triggers tighter monetary conditions, substantiating the need for a higher real interest rate profile in SA.

Notwithstanding a muted domestic growth outlook, we expect interest rates to be hiked by 75 basis points this year, followed by a further 50 basis points over the course of 2017 to combat rising inflation pressures and a deterioration in inflation expectations. Based on our expectations for inflation, this would allow real interest rates to stay in positive territory both this year and next, averaging just below 1.0% between 2016 and 2017.





*Herman van Papendorp*
**Head: Macro Research and Asset Allocation**
Momentum Investments



*Sanisha Packirisamy*
**Economist**
Momentum Investments


# The investment case for commercial real estate in frontier Africa

By David Lashbrook

We believe that the commercial real estate asset class in frontier Africa (i.e. Africa ex South Africa) provides investors with an attractive investment opportunity that has the potential to deliver meaningful positive real returns over the medium term. Investors who have invested in the South African commercial real estate markets over the last 15 years have been handsomely rewarded as markets matured, liquidity deepened and yields compressed accordingly.

We believe that the frontier Africa real estate markets are now at the same stage as the South African real estate market was at the turn of the century. The first REITS and institutional buyers are just beginning to emerge, which (if we follow the South African example), should lead to an increase in transactions and liquidity; these factors will hopefully result in a compression in yields over the medium term.

Commercial real estate developers are currently able to deliver commercial real estate developments in Africa at double digit yields. Rentals are typically in US dollars, or at least referenced to dollars. These double digit dollar yields are likely to be of interest to investors when compared with the single digit yields in rands currently available in the South African commercial real estate market. The higher yields in Africa are largely the product of an imbalance in demand and supply. Each of these factors is discussed in more detail below.

## Supply

On the supply side, there is limited availability of land held in terms of clean, uncontested title with suitable development rights. In addition, few developments of international standard are completed. The shortage of clean land and investment quality properties can be attributed to the following factors:

• Most cities in Africa, outside of Southern Africa, were designed and built under the colonial occupation with much lower population numbers in mind, and without catering for the effect of urbanisation. As these countries gained independence, many of them experienced successive changes in their respective governments resulting in a lack of continuity, skills and focus on urban design. This ultimately led to a shortage of planned developable areas.

• Another consequence of ongoing regime changes was that land ownership became increasingly more difficult to ascertain through each cycle. This resulted in many claimants for a single piece of land. Land acquisition is further frustrated by a lack of records to identify real ownership.

• The existence of rapid uncontrolled urbanisation into the cities (due to poverty in the rural areas) has also made unoccupied, clean land scarce.

• Opportunities for retail development are often complicated by the fact that retail facilities require much larger tracts of land due to the lower density achieved, or bulk used in these developments. These large properties are typically extremely difficult to find in the cities.

• Land consolidation is not always possible as the sale of land in some cultures is perceived as a weakness and therefore frowned upon.

• Certain old residential areas have become sought after for commercial offices and up-market residential premises. In many cases where land is available, ownership remains an issue as the land is traditionally held by a family and not a legal entity. Any sale of land would require the approval of all the family members. Often the members are diverse and widespread and it is not entirely clear who the family members are.

• Limited sophistication of financial systems has resulted in land owners often being unable to obtain debt financing to develop their land, which has subsequently forced them to use equity only to build developments. This results in fewer developers in these markets and less competition when it comes to the pricing of the final product.

• The risk of developing in an environment where regulatory red tape can cause delays, as well as the high start-up costs (travel, local company structures, and legal fees) reduces the number of developers investigating and operating in these markets.

• The lack of efficient town planning systems creates a short supply of valid development rights. Many African countries lack the development skills, know-how and resources required in order to meet international expectations of quality work and management. Resources include skilled labour, machinery and building materials. This has resulted in a shortage of high quality developments that meet international standards.

## Demand

• Favourable demographics provide a strong tailwind for future economic growth and investment in African real estate. For example, Nigeria has a total population of around 170 million with the number of people living in Lagos estimated at 18 million. Nigeria has a large and growing middle class which bodes well for sustainable long-term growth in the real estate sector. The same fundamentals apply to other cities and countries targeted by the Fund, such as Maputo in Mozambique and Accra in Ghana.

• Not only is the population getting larger and richer, but it is progressively moving into the cities and towns. Sub-Sahara Africa's urban population is expected to treble from just over three hundred million people today to one billion by 2050. These people will require somewhere to live, somewhere to work and somewhere to shop.

• Massive retail gaps exist. For example, the greater Johannesburg area, with a population of 8 million, has eighty four retail malls comprising a minimum of 24,000m² each. Lagos on the other hand has a population of approximately 18 million and two shopping malls. Accra has a population of 2 million and two malls. The greater Maputo area has a population of 2 million and has no regional sized shopping malls.

• Industrial space close to city centres is in short supply. More specifically, there is an increasing need for logistics operations as retailers expand into new territories.

• Lack of road and public transport infrastructure creates demand for residential living space close to work locations. Areas that have infrastructure are limited and consequently command higher values.

## Conclusion

The discussion of the supply and demand above highlights the fact that investing in Africa is not without its challenges. However, these are not insurmountable and can be mitigated by investing with an experienced team and by local partnership formation. And, if a moderate amount of leverage is added to the double digit dollar yields currently available, we believe that the frontier African real estate asset class has the potential to deliver meaningful returns over the medium term.

David Lashbrook
**Head: Africa Investment Strategies**
Momentum Global Investment Management

# Momentum Investments market commentary for the quarter ending December 2015

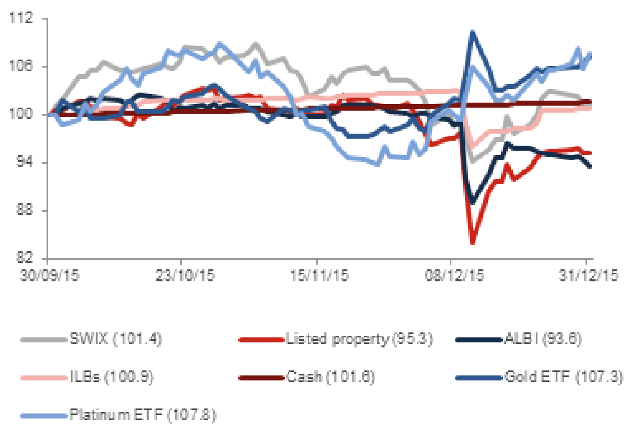
by Herman van Papendorp and Sanisha Packirisamy

### Plummeting rand drives asset class performance in 4Q15

A confluence of factors caused the rand to fall steeply during the final quarter of 2015. Firstly, rising evidence of the inevitability of the first US rate hike in almost a decade, coupled with further easing measures in Europe and Japan, propelled the US dollar stronger in the quarter, with negative consequences for the currencies of commodity exporters with large current account deficits like South Africa (SA).

Furthermore, slowing domestic growth, culminating in negative credit rating actions by both Fitch and S&P in early December, put additional pressure on the rand. But the rand's inherent vulnerability was fully exposed when SA changed finance ministers twice in the space of five days in December, derailing previous views that SA's monetary (Reserve Bank) and fiscal (Treasury) institutions were above political meddling.

**Chart 1: SA asset class performance in 4Q15 (indexed)**




*Source: INET BFA, Momentum Investments*

The more than 10% rand decline against the US dollar during 4Q15 was clearly reflected in the relative performance of asset classes in the quarter. Unsurprisingly, the best performers were global assets, with global equities outperforming global bonds and cash. Among the local asset classes, the rand's weakness also assured outperformance from the gold and platinum ETFs, despite declining commodity prices.

Domestic cash outperformed equities and ILBs during the quarter. Within equities, non-mining rand hedge shares strongly outperformed, which was reflected in the outperformance of Industrials (+6.6%) over Financials (-3.3%) and Resources (-19.2%). With rand weakness impacting negatively on inflation and interest rate expectations, local bonds (10-year yields up by 130 bps in the quarter) and listed property were by far the worst performers during 4Q15.

### 2016 again a year for full global investment exposure

We believe investors should maintain a full exposure to offshore assets in 2016, with the fundamentals and valuations of global equities looking far superior to those of global fixed income assets. Although there seems to be little to choose between developed market (DM) and emerging market (EM) equities on valuation grounds, we believe superior fundamentals for the former skew the risk-reward ratio meaningfully in favour of DM equities, particularly vis-à-vis commodity exporting and current account-deficit EMs. Within the DM equity space, the combination of positive macro-economic realities and preferable valuations support excess exposure to the European and Japanese equity markets, rather than to the US and UK.

Among SA asset classes, we believe the SA equity market's valuation premium relative to its own history and other emerging markets is justified by the higher quality of its earnings base, as well as the supremacy of its management teams and corporate governance. In contrast to the opening up of a valuation discount in the SA bond market that has increased the attractiveness of this asset class, the huge valuation premium attached to local listed property constrains its prospective returns, in our view. On a risk-adjusted basis, returns from domestic cash look enticing to us in the near term.

## Shallow and uneven global economic recovery

2016 is likely to be characterised by a further desynchronisation in growth and policy in major global economies. A sturdy growth outlook and stable inflation expectations will likely prompt central banks in the United States (US) and United Kingdom to nudge monetary policy rates higher from ultra-low levels, while significantly negative output gaps, fragile growth trajectories and benign inflation expectations point to the likelihood of the European Central Bank (ECB) and Bank of Japan (BoJ) maintaining an easing bias for time to come.

With US job creation averaging more than 220 000 per month in 2015 and headline unemployment dropping to 5%, a consumption-led recovery is expected to leave the world's largest developed economy as the relative bright spot globally. This is in spite of sluggish global demand and a firm US dollar holding back a faster acceleration in export and investment growth. Domestic demand, services and residential construction have displayed resilience to weakness in global activity, suggesting that the US economy is on a firm enough footing to gradually step away from ultra-accommodative monetary policy. Nevertheless, tighter monetary conditions from a stronger greenback, benign wage inflation and the threat of negative spill over effects from a bumpy global economic recovery suggest that US Federal Reserve (Fed) officials will move more cautiously than during past rate hiking cycles, which could keep the target federal funds rate below "normal" levels for quite some time.

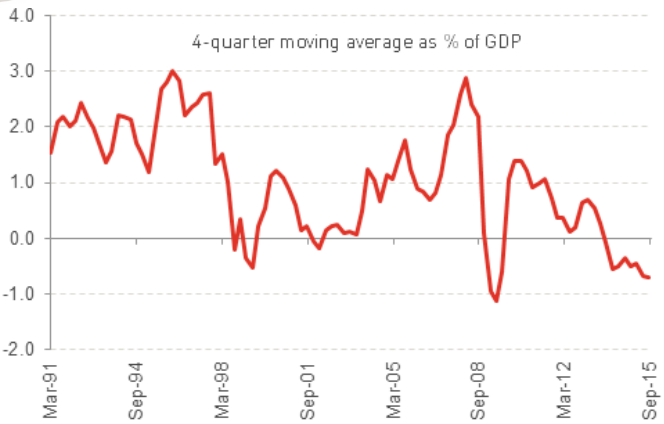
In contrast, fresh ECB action in December 2015 was deemed necessary to spur price pressures and drive export growth higher in the Eurozone. Yet, even with this level of unprecedented easing, stimulus efforts only amount to roughly 15% of Eurozone GDP, much lower than the 25% of GDP stimulus previously induced by the likes of the Fed or the Bank of England (BoE). As a result, further easing measures may have to be announced in 2016 in the event of further disappointments in growth and inflation prints. Though GDP likely expanded at a reasonable 1.5% for the region as a whole in 2015, outside of Spain, activity remained disappointing in Germany and continued to lag in France and Italy. We expect a mild expansion in Eurozone growth to be carried by domestic demand in 2016 as low oil prices, a slow recovery in credit growth and easy monetary policy boost consumption spend, while a weaker euro continues to keep peripheral economies competitive. Near-term growth could also benefit from a rise in public expenditure in response to the rising number of asylum seekers, but intensified geopolitical risks remain a threat to trend growth in the longer run.

Whereas the recovery in developed markets continued to gain traction over 2015 (thanks to healing labour and credit markets and still accommodative fiscal and monetary policy settings, which supported firmer domestic demand), a deceleration in capital flows, pressured commodity prices and tepid growth in global trade drove a continued deceleration in growth in emerging economies to its lowest level since the global financial crisis. At an estimated 4.3%, 2015 growth in EMs printed well below the average observed over the early 2000s.

While rapid growth in the so-called BRIC nations (Brazil, Russia, India and China) had previously shored up global growth, given its sizeable c.30% contribution to world GDP, its synchronous deceleration since 2010 (with India being the exception due to robust investor sentiment and buoyant growth in real incomes) has contributed to the slowdown in other emerging economies. In a recent report, the World Bank highlighted the possible adverse effects on global GDP from a growth slowdown in BRIC. A 1% sustained decline in growth in BRIC could reduce economic activity in other EMs by around 0.8% and could shave nearly 0.4% off from overall global growth.

Lingering EM vulnerabilities suggest that challenging growth conditions are likely to persist. Domestically, depleted fiscal buffers, rising private sector leverage and waning productivity growth could limit the recovery in EMs in 2016, particularly as less favourable external financing conditions (see chart 2), a poor business climate and domestic policy tightening in key markets have reinforced obstacles to higher investment and growth.

**Chart 2: Sharp slowdown in capital flows to EM ex-China**




*Source: Capital Economics, Momentum Investments*

Rising interest rate prospects for the US imply tighter monetary conditions for emerging economies, particularly those running extended current account deficits and/or those sporting hefty dollar-debt burdens. While rising domestic interest rates on the back of potential currency weakness may attempt to partly negate the effect of declining portfolio flows, a weak growth backdrop may limit the extent of EM rate hikes, while higher inflation could push real rates lower.

Natural resource producers and economies with strong trade linkages to China have endured the hardest hit on growth. The latest (official) GDP data indicates that growth in the Asian behemoth lost momentum from the average 9.8% rate observed since 1980, to 6.9% more recently in 3Q15. The deceleration in growth proved to be most visible in sectors with considerable overcapacity, namely manufacturing and real estate, while activity in the consumption and services-related sectors held up reasonably well. Growth in China is likely to slow further over the next five years as Chinese officials implement their plan to reorient GDP to a more sustainable and balanced model. In an environment where China re-aligns its growth profile away from infrastructure and export-led GDP towards less trade-intensive consumption and services, we are unlikely to see commodity prices staging a sharp recovery. An overhang in the global supply of key commodities further points to little support for a significant reacceleration in commodity prices in the coming years.

Though there is a potential for India to take up China's mantle as possibly the next dominant player in world commodity demand in the future, growth in India's commodity consumption over the next ten years is unlikely to replicate the positive demand shock created by China over the past decade and a half. India's current contribution to global commodity consumption remains a fraction of that of China's. Furthermore, India's democratic rule of law hinders a faster acceleration in the rollout of commodity-intensive infrastructure projects, thereby capping demand.

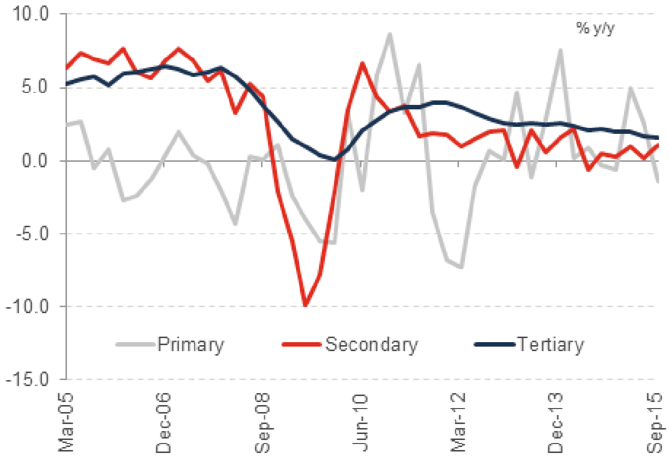
In this context, net commodity-exporting countries, particularly those facing large external imbalances, are likely to face a less favourable terms-of-trade trajectory, suppressing economic growth prospects over the next while. Furthermore, growth is likely to be least resilient to any negative shocks in those developing nations that have failed to address shortfalls in governance and labour markets through the implementation of structural reforms.

## Lacklustre growth in SA faces mounting headwinds

Trend growth in SA has tumbled from its longer-term historical rate of above 3% to below 2% as the private sector refrains from embarking on substantial new fixed investment in light of muted global and domestic economic activity, binding energy constraints and heightened investor unease over domestic economic policy direction. Rising fiscal pressures, a dismal employment outlook and a dip in real wages are likely to inhibit a faster acceleration in consumption spend in 2016, while the export benefit of a weaker rand is likely to be curbed somewhat by fragile global trade activity and rising input costs.

Consequently, real growth in SA is likely to continue underperforming our estimate of potential growth in 2016, expanding at a rate only marginally higher than 1.0%. Growth rates in SA's primary and secondary sectors have been punctured by soft global commodity prices and subdued demand both globally and locally (see chart 3). Dry and hot weather conditions further threaten to shave off between 0.5% and 1.0% from GDP this year should agricultural volumes be hit in excess of 20%. Morgan Stanley estimates that the negative impact of the drought could further trim SA exports by around USD9.5 billion. As a result of lower domestic agricultural output, higher food imports are expected to partly negate the impact of slowing import demand as weak local demand and a higher rand price of foreign produced goods curb consumer imports.

**Chart 3: GDP headwinds intensifying outside tertiary sector**




*Source: Stats SA, Global Insight, Momentum Investments*

Global investors withdrew USD52 billion from EM equity and bond funds in 3Q15 on rising risk aversion, registering the largest quarterly outflow on record. This has led to an increase in currency pressures for commodity exporters with large external deficits in particular, while idiosyncratic political and sovereign downgrade risks have aggravated SA currency moves.

Significant currency depreciation (and volatility) intensifies the possibility of an extended inflation breach despite the weaker currency pass through observed in SA to date. The SA Reserve Bank (SARB) has warned that the recent convergence in medium-term inflation expectations (by analysts, firms and trade unions) at close to the upper end of the 3% - 6% inflation target band further threatens higher price setting in the economy. With inflation threatening to breach the upper target of 6% on average this year, we expect 75 basis points worth of rate rises over the course of 2016 to keep inflation expectations anchored and real policy rates in positive territory, particularly against the backdrop of further interest rate hikes by the Fed in response to firmer US growth.

A more benign structural growth outlook and shrinking fiscal buffers leave SA's fiscal authorities with less room to manoeuver, jeopardising Treasury's fiscal consolidation timeline and medium-term debt stabilisation plan. The nature of SA's fiscal expenses remains highly structural. An escalating public service wage bill and rising debt servicing costs have crowded out other forms of more beneficial growth enhancing spend and remain a trigger for further negative sovereign ratings action towards sub-investment grade status.

Doubts around the direction of economic policy have discouraged inward investment. This limits trend growth and hence revenue collections on a more sustainable basis, restricting SA's ability to grow its way out of a potential debt crisis in the absence of another commodity supercycle.

Earlier student protests, the recent finance ministry debacle and inaction to reduce maladministration in SA's state-owned corporations have raised concerns over government's ability to deal with socio-political and economic challenges. Endorsing policy measures that could damage the investment climate could further taint SA's investment grade status. If government does not react to growing fiscal risks in time, further expected cuts to longer-term capital expenditure in favour of current spend will exacerbate benign domestic growth projections, eventually forcing government debt ratios even higher. A larger debt burden, reduced sovereign creditworthiness and lower inward investment would perpetuate a poor growth environment, fuelling a weak growth-high debt spiral.



*Herman van Papendorp*
**Head: Macro Research and Asset Allocation**
Momentum Investments

*Sanisha Packirisamy*
**Economist**
Momentum Investments

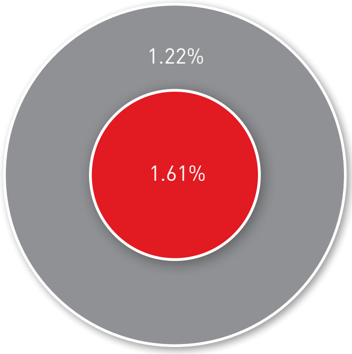
# Partially Vesting Smooth Bonus Range | Multi-Manager Smooth Growth Fund Global

## Fund Snap Shot

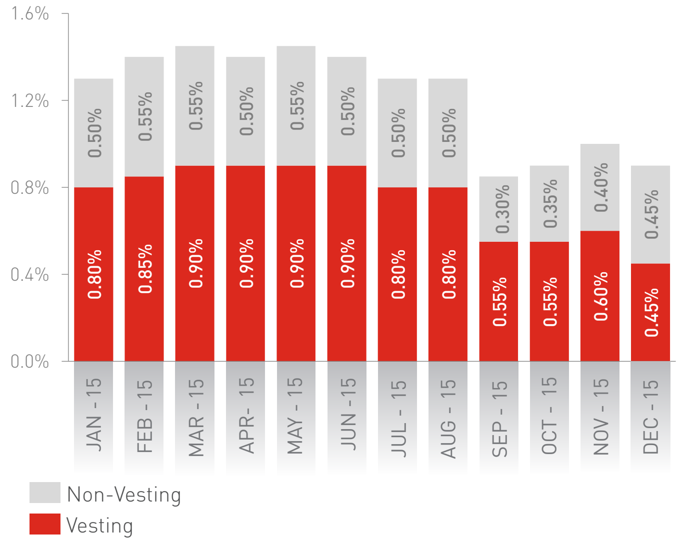
| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE | ANNUALISED 3-YEAR VOLATILITY OF BONUSES | ANNUALISED 3-YEAR UNDERLYING ASSET RETURN |
|---|---|---|---|---|
| Jan 2004 | 102.5% - 107.5% | R12.0bn | 0.85% | 15.56% |

## Performance

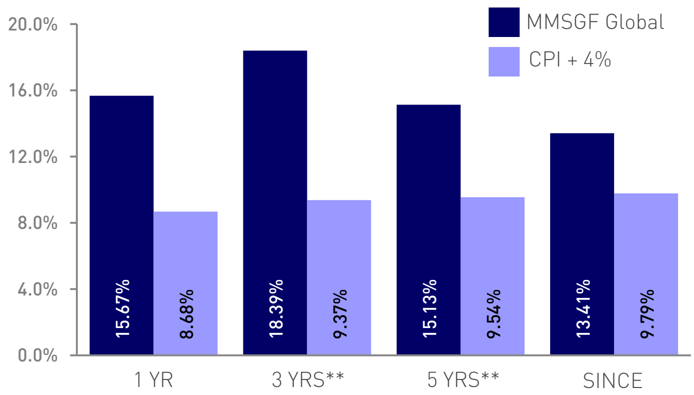
The total bonus* for the past quarter on the Multi-Manager Smooth Growth Fund Global is shown below.




The chart below shows the monthly bonuses* for the past 12 months




The chart below shows the long term bonus* performance of the Multi-Manager Smooth Growth Fund Global against CPI + 4%



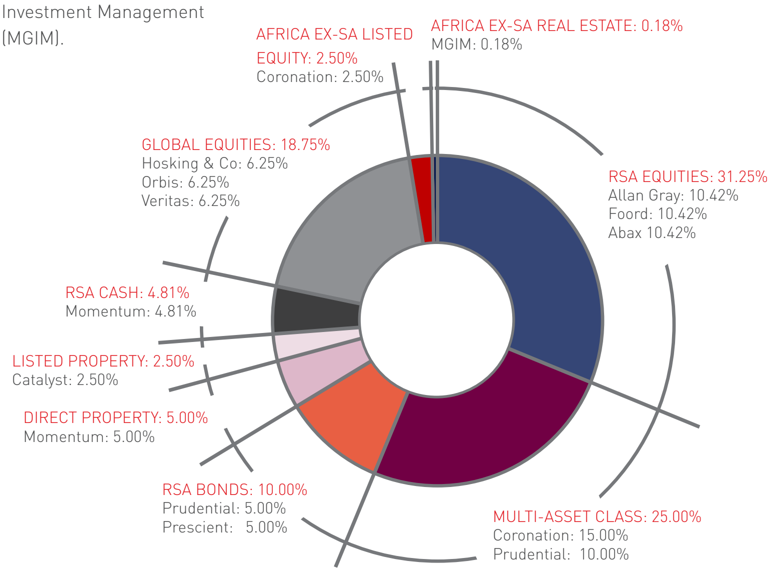

*CPI figures are lagged by two months*

* Bonuses are net of all charges except for the fixed investment management fee

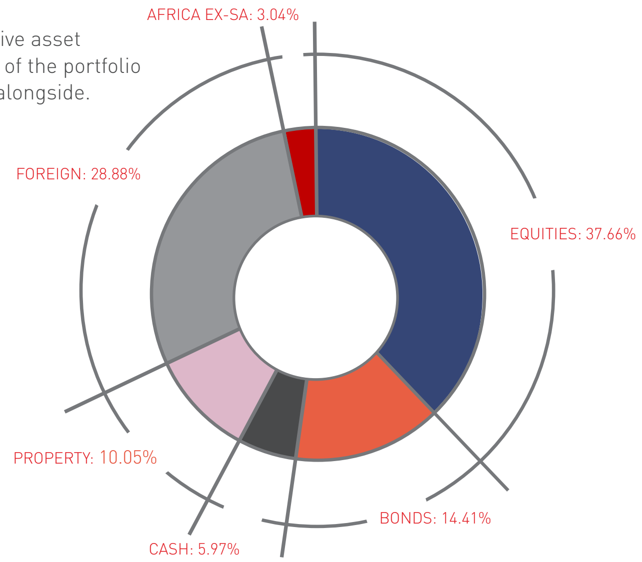
** Annualised

## Asset Allocation

The strategic asset allocation was changed during the quarter. The new Africa ex-SA Real Estate allocation was funded by RSA cash. This allocation is expected to increase gradually over the next 5 years to a total of 2.50%, in line with drawdown notices from Momentum Global Investment Management (MGIM).




The effective asset allocation of the portfolio is shown alongside.




From the fifteenth century, **mariners' astrolabes** were used to determine the latitude of a ship at sea. Designed for use on boats in rough water and heavy winds, the astrolabe could locate and predict the positions of the sun, moon, stars and planets, determining local time given local latitude and vice-versa. Less than one hundred are known to have survived from antiquity.

In the new world, Trustees, Professional Financial Advisors and members need clear directions to stay on track within the turbulent retirement fund environment. Our best-of-breed multi-manager smooth bonus products with independent governance provide just that.

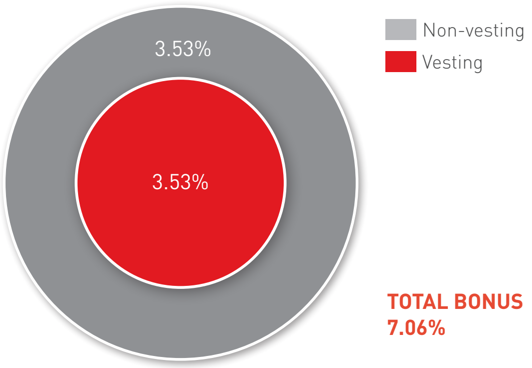
# Partially Vesting Smooth Bonus Range |
## Multi-Manager Smooth Growth Fund Local

### Fund Snap Shot

| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE | ANNUALISED 3-YEAR VOLATILITY OF BONUSES | ANNUALISED 3-YEAR UNDERLYING ASSET RETURN |
|---|---|---|---|---|
| Jan 2004 | > 120% | R 164m | 1.49% | 10.58% |

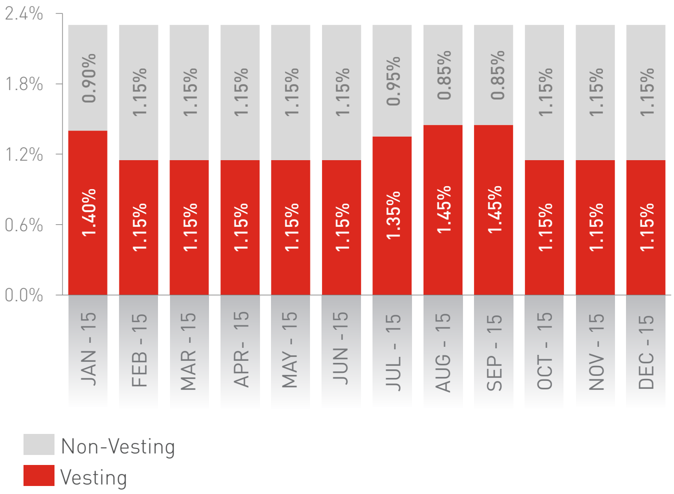
### Performance

The total bonus* for the past quarter on the Multi-Manager Smooth Growth Fund Local is shown below.

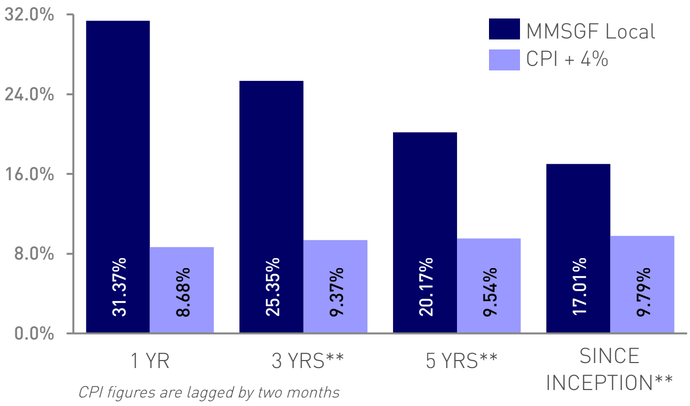



**TOTAL BONUS 7.06%**

The chart below shows the monthly bonuses* for the past 12 months.

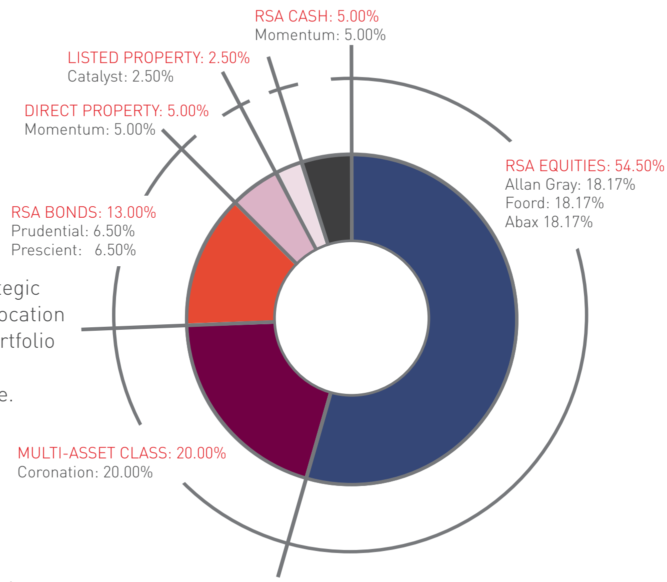



The chart below shows the long term bonus* performance of the Multi-Manager Smooth Growth Fund Local against CPI + 4%



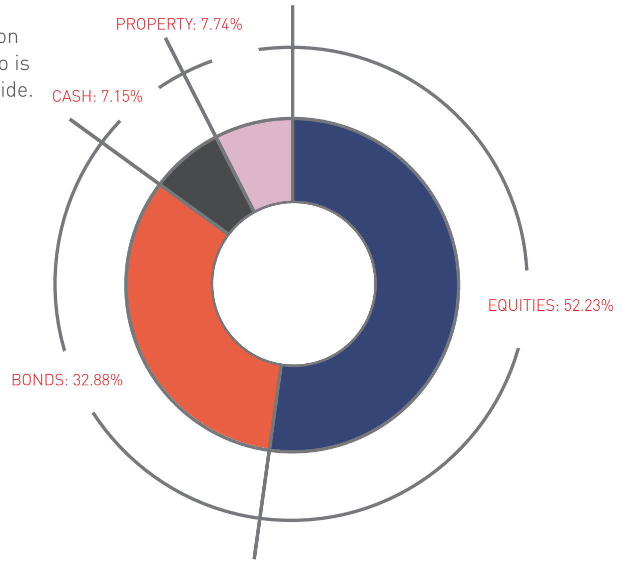

* Bonuses are net of all charges except for the fixed investment management fee
** Annualised

### Asset Allocation




The strategic asset allocation of the portfolio is shown alongside.

The effective asset allocation of the portfolio is shown alongside.




From as early as 150 B.C navigators could find their latitude, but ships were lost in shipwrecks because it was impossible to determine longitude. Thanks to **the 17th century sextant**, the navigator could measure the angle between the moon and a celestial body, calculating the exact time at which this distance would occur. Knowing the time meant knowing the longitude.

In the new world, Trustees, Professional Financial Advisors and members need certainty on their journey to financial wellness. Expert guidance from the thought leaders means knowing where you're heading and how to get there.

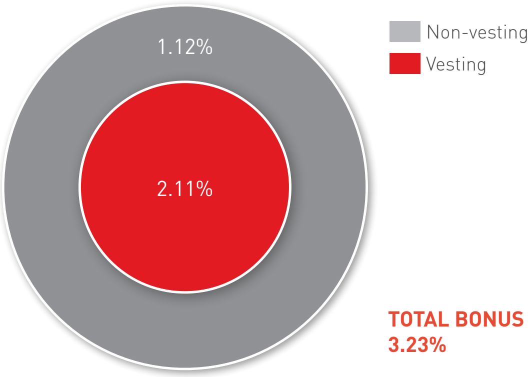
# Partially Vesting Smooth Bonus Range | Smooth Growth Fund Global

## Fund Snap Shot

| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE | ANNUALISED 3-YEAR VOLATILITY OF BONUSES | ANNUALISED 3-YEAR UNDERLYING ASSET RETURN |
|---|---|---|---|---|
| Jan 1989 | 102.5% - 107.5% | R 2.7bn | 1.04% | 11.84% |

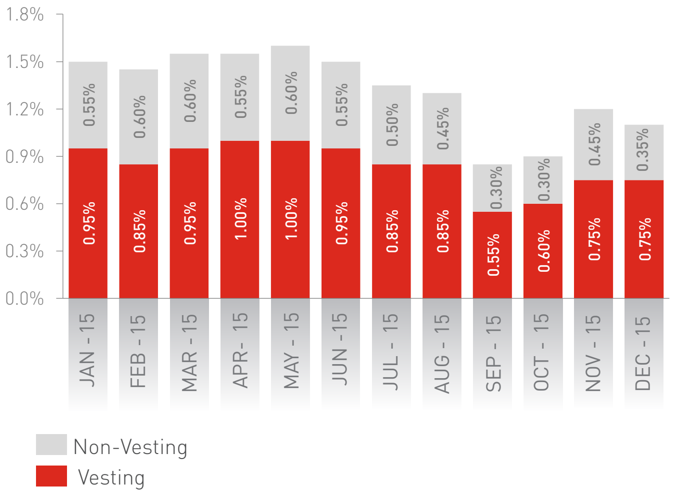
## Performance

The total bonus* for the past quarter on the Smooth Growth Fund Global is shown below.

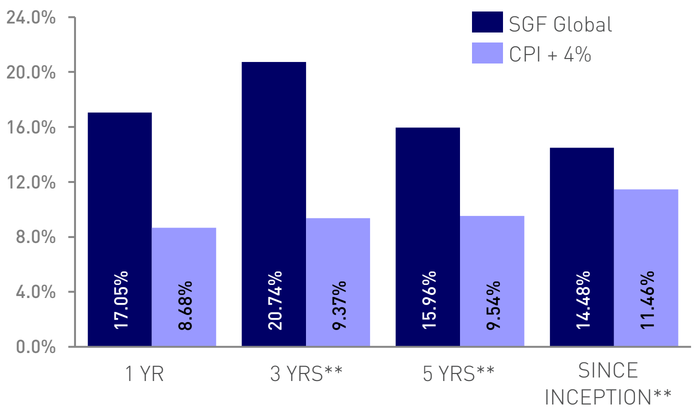



**TOTAL BONUS 3.23%**

The chart below shows the monthly bonuses* for the past 12 months.




The chart below shows the long term bonus* performance of the Smooth Growth Fund Global against CPI.



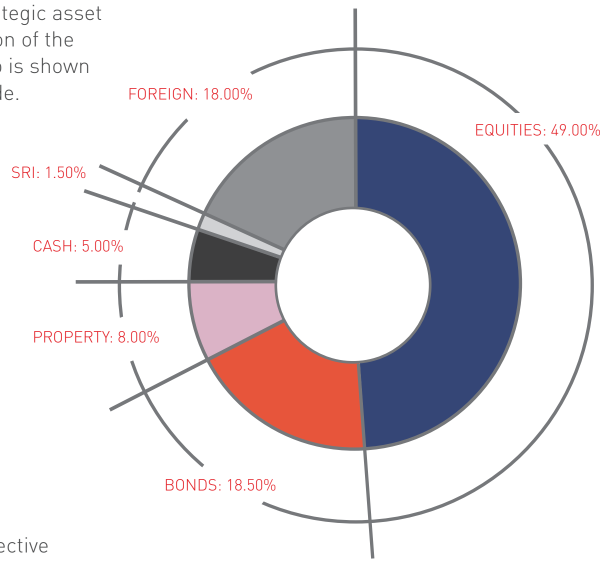

*CPI figures are lagged by two months*

* Bonuses are net of all charges except for the fixed investment management fee

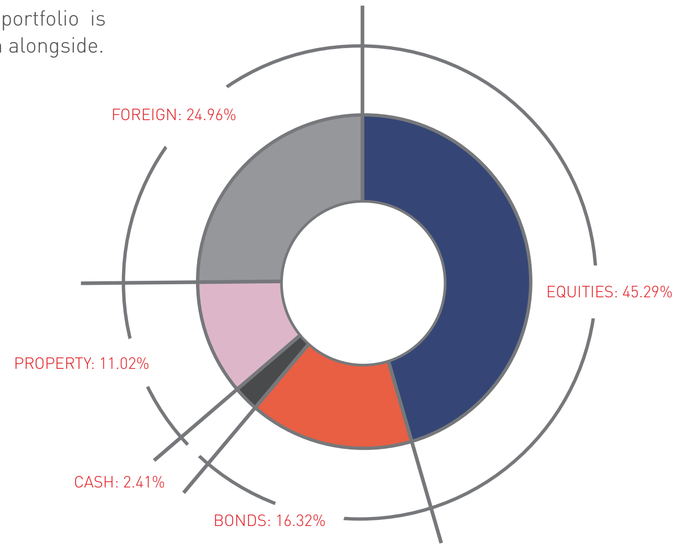
** Annualised

## Asset Allocation

The strategic asset allocation of the portfolio is shown alongside.




The effective asset allocation of the portfolio is shown alongside.




**The engine order telegraph** is used by the pilot on the bridge to instruct the engine room below to power the vessel at the right speed. By moving the handle to a different position on the dial, a bell would ring in the engine room and move their pointer to the same position - a fast and very handy way of powering the vessel away from trouble.

In a world where Trustees, Professional Financial Advisors and employees are looking for greater certainty, Momentum's continuous capital guarantee on benefit payments and smooth inflation-beating returns will result in plain sailing.

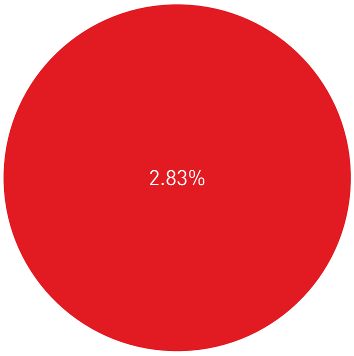
# Fully Vesting Smooth Bonus Range | Multi-Manager Secure Growth Fund

## Fund Snap Shot

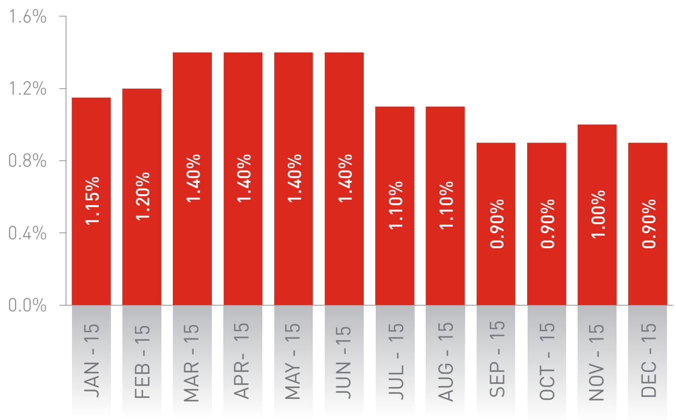
| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE | ANNUALISED 3-YEAR VOLATILITY OF BONUSES | ANNUALISED 3-YEAR UNDERLYING ASSET RETURN |
|---|---|---|---|---|
| Nov 2007 | 107.5% - 112.5% | R 47m | 0.70% | 13.08% |

## Performance

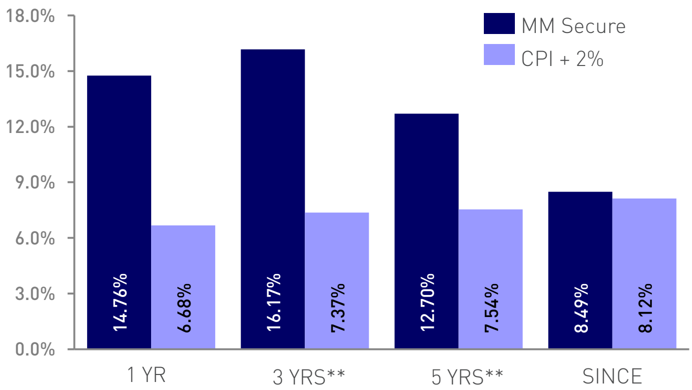
The total bonus* for the past quarter on the Multi-Manager Secure Growth Fund is shown below.




The chart below shows the monthly bonuses* for the past 12 months.




The chart below shows the long term bonus* performance of the Multi -Manager Secure Growth Fund against CPI + 2%

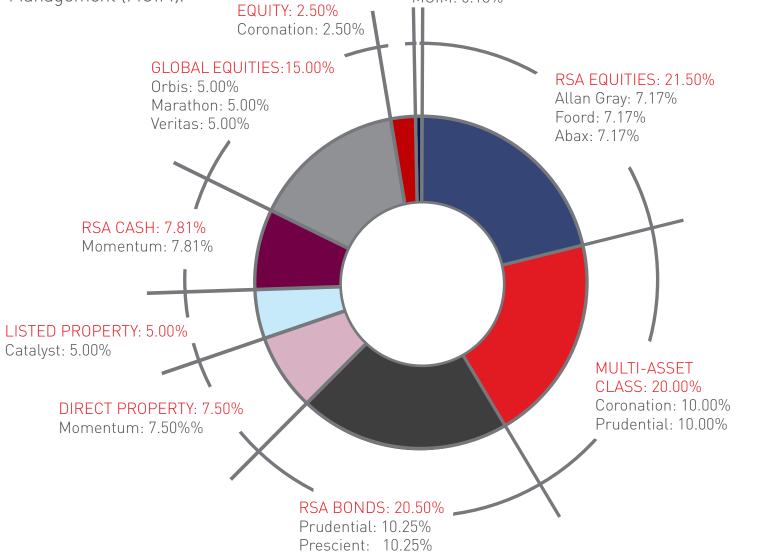



*CPI figures are lagged by two months*

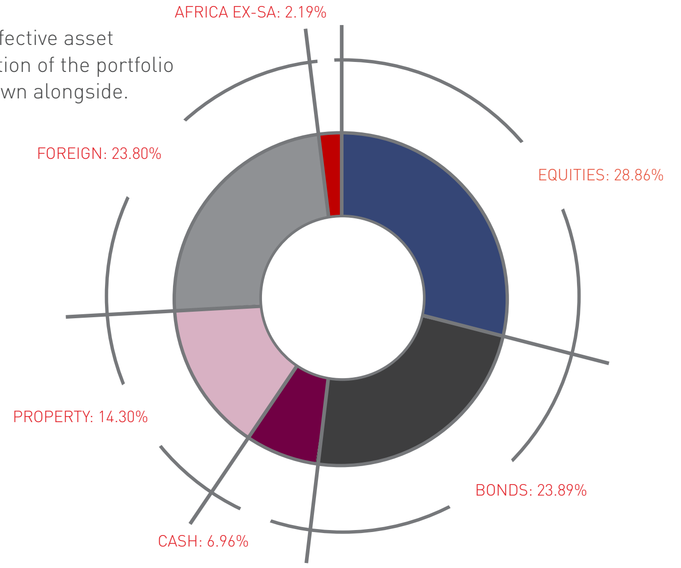
* Bonuses are net of all charges except for the fixed investment management fee
** Annualised

## Asset Allocation

The strategic asset allocation was changed during the quarter. The new Africa ex-SA Real Estate allocation was funded by RSA cash. This allocation is expected to increase gradually over the next 5 years to a total of 2.50%, in line with drawdown notices from Momentum Global Investment Management (MGIM).




The effective asset allocation of the portfolio is shown alongside.




The first known **practical telescope** was invented in the Netherlands at the beginning of the 17th century. A telescope aids in the observation of remote objects by collecting electromagnetic radiation (including visible light), using glass lenses to increase the apparent size and brightness of distant objects.

Clarity is a key need of Trustees, Professional Financial Advisors and employees. Our transparent approach to bonus declarations and capital guarantees provide peace of mind on the journey to financial wellness.

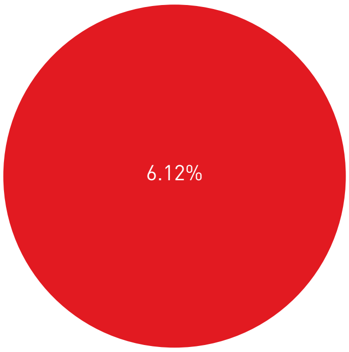
# Fully Vesting Smooth Bonus Range |
## Multi Manager Secure Growth Fund Bonus Series 2013

### Fund Snap Shot

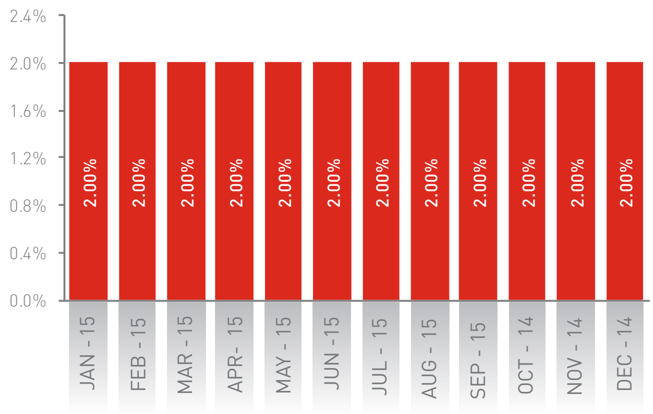
| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE |
|---|---|---|
| Jun 2013 | > 120% | R 56m |

### Performance

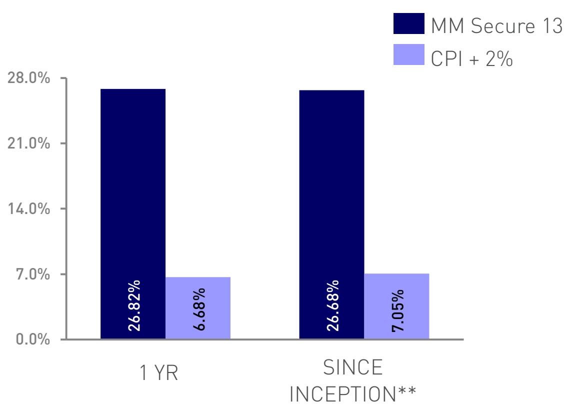
The total bonus* for the past quarter on the Multi Manager Secure Growth Fund Series 2013 is shown below.




The chart below shows the monthly bonuses* for the past 12 months.




The chart below shows the long term bonus* performance of the Multi -Manager Secure Growth Fund Bonus Series 2013 against CPI + 2%

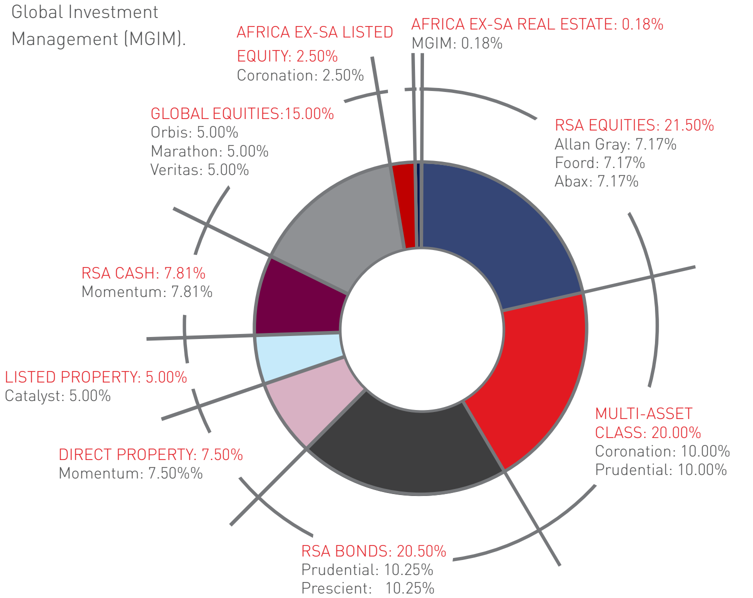



*CPI figures are lagged by one month*

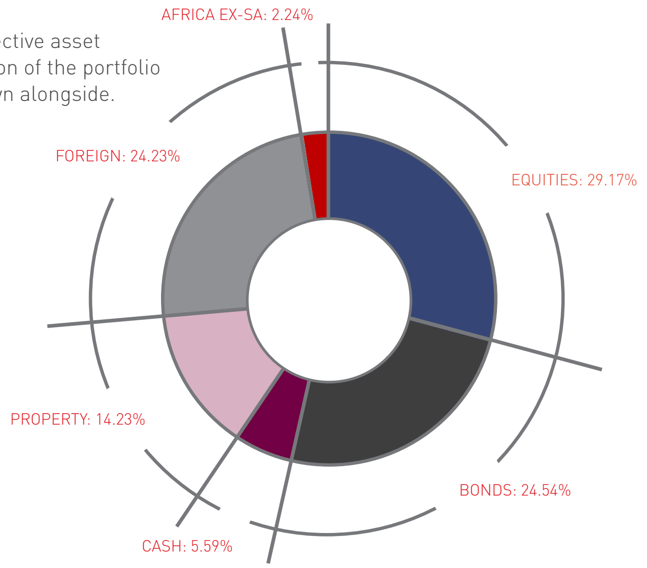
* Bonuses are net of all charges except for the fixed investment management fee
** Annualised

### Asset Allocation

The strategic asset allocation was changed during the quarter. The new Africa ex-SA Real Estate allocation was funded by RSA cash. This allocation is expected to increase gradually over the next 5 years to a total of 2.50%, in line with drawdown notices from Momentum Global Investment Management (MGIM).




The effective asset allocation of the portfolio is shown alongside.




Following the invention of the telescope in the 17th century, the advantages of mounting two of them side by side for binocular vision became obvious. Developed by Italian optician, Ignazio Porro in 1854 and made popular by the Carl Zeiss Company in the 1890s, **Binoculars** give users a three-dimensional image, presented to each of the viewer's eyes from slightly different viewpoints. This merged view provides a greater impression of depth.

We recognise that in the new world, nothing less than 100% certainty will do. As a result, our rigorous portfolio construction inspires investor confidence in the prospective investment performance of the Fund.

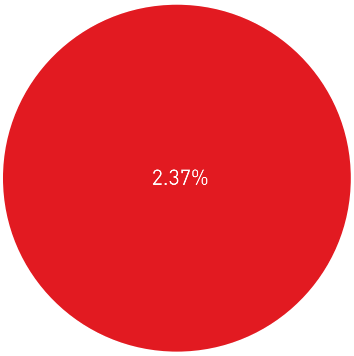
# Fully Vesting Smooth Bonus Range | Capital Plus Fund

## Fund Snap Shot

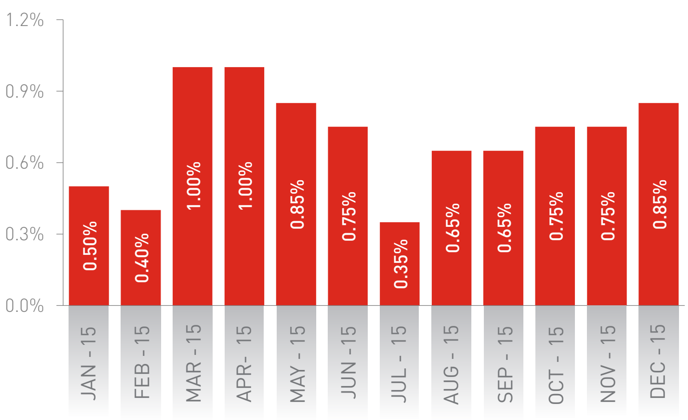
| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE | ANNUALISED 3-YEAR VOLATILITY OF BONUSES | ANNUALISED 3-YEAR UNDERLYING ASSET RETURN |
|---|---|---|---|---|
| Mar 2005 | 100% - 105% | R 322m | 0.77% | 8.97% |

## Performance

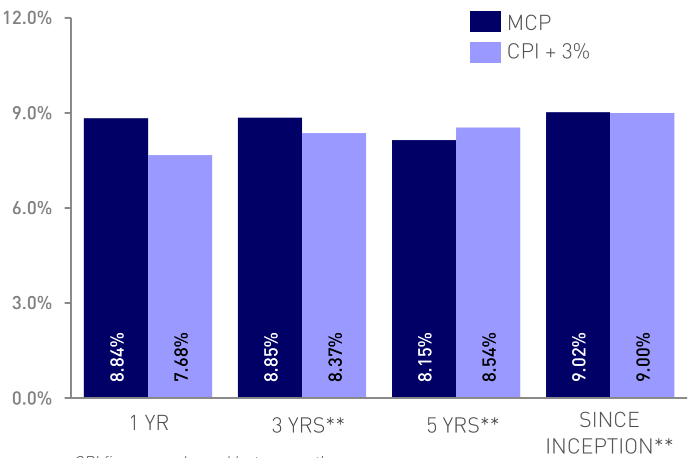
The total bonus* for the past quarter on the Capital Plus Fund is shown below.




The chart below shows the monthly bonuses* for the past 12 months.




The chart below shows the long term bonus* performance of the Capital Plus Fund against CPI + 3%

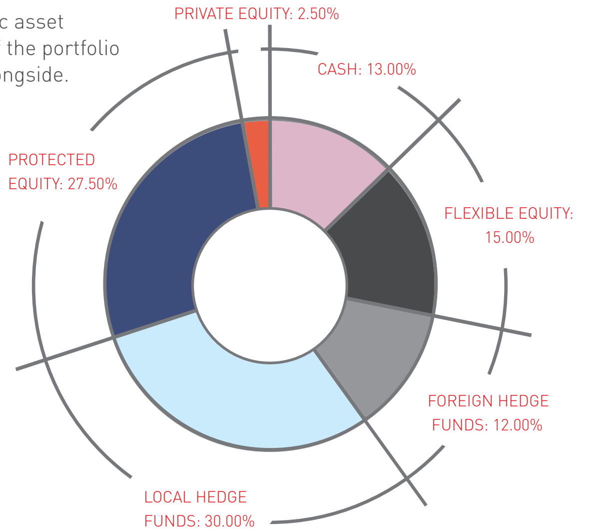



*CPI figures are lagged by two months*

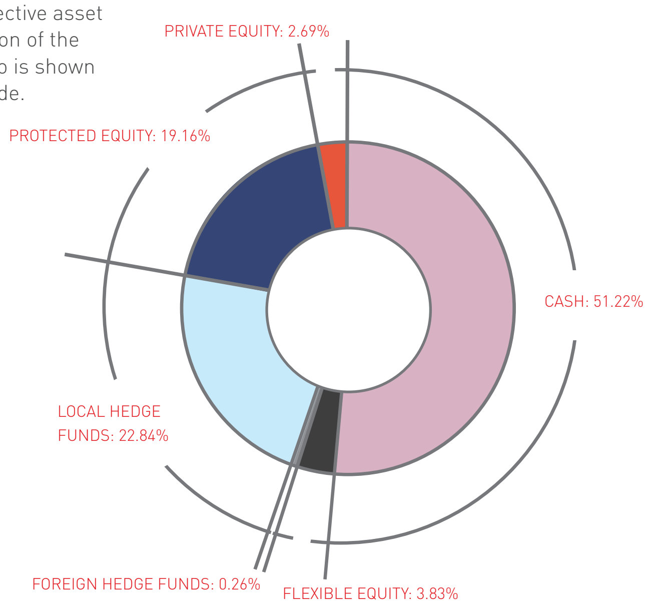
* Bonuses are net of all charges
** Annualised

## Asset Allocation

The strategic asset allocation of the portfolio is shown alongside.




The effective asset allocation of the portfolio is shown alongside.




Thank Greek astronomy for establishing the sphericity of the earth in the 3rd century BC. Flat maps use a map projection that inevitably introduces an amount of distortion.

**A terrestrial globe** is the only representation of the earth that does not distort the shape or size of large features.

The oldest surviving one was created by Martin Behaim in Nuremberg in 1492.

When it comes to leading the industry, it helps to have an accurate 360 degree view. Which is why our innovative, value-for-money products are redefining the landscape of financial wellness, for Trustees, Professional Financial Advisors and members.

# Fully Vesting Smooth Bonus Range |
## Smart Guarantee + 3 Fund

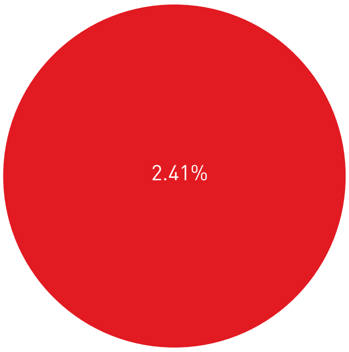
### Fund Snap Shot

| INCEPTION DATE | FUNDING LEVEL RANGE | FUND SIZE | ANNUALISED 3-YEAR VOLATILITY OF BONUSES | ANNUALISED 3-YEAR UNDERLYING ASSET RETURN OF BONUS GENERATING PORTFOLIO |
|---|---|---|---|---|
| Oct 2013 | 102.5% - 107.5%[1] | R 146m | 1.14%[2] | 11.94% |

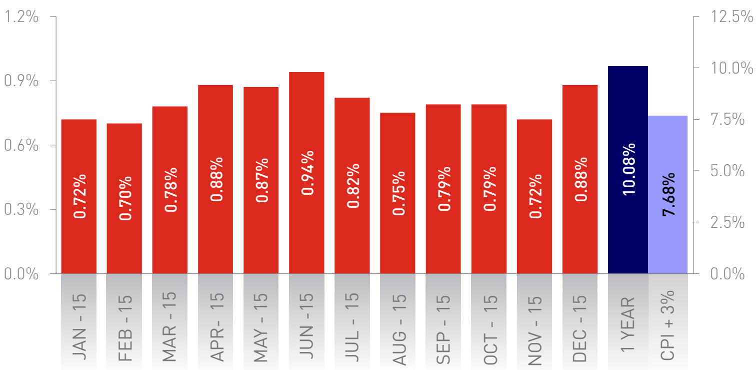
[1] See 'Bonuses to be declared' paragraph below
[2] Figures are based on back-tested (not actual) bonuses.

### Performance

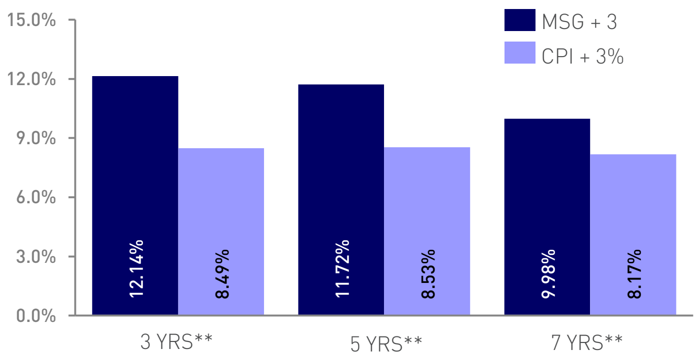
The total bonus* for the past quarter on the Smart Guarantee + 3 Fund is shown below.




The chart below shows the actual monthly bonuses* for the past 12 months, together with the actual one year performance* against the benchmark of CPI +3%.




The chart below shows the long term back-tested performance* of the Smart Guarantee +3 Fund against CPI + 3%.

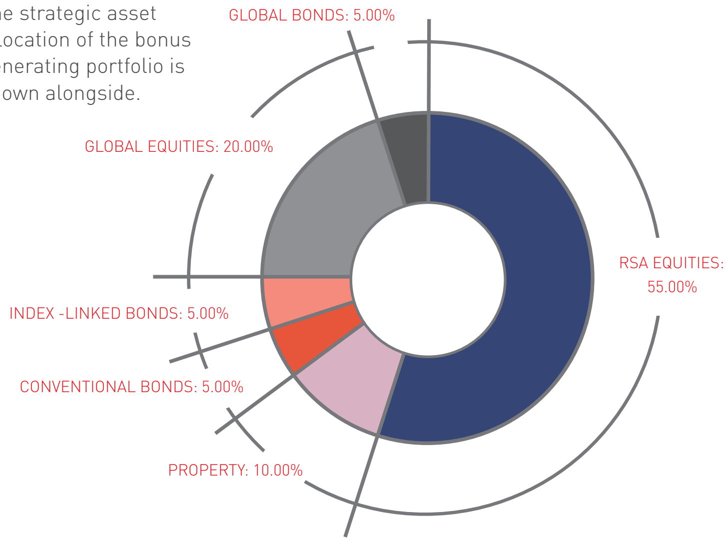



*CPI figures are lagged by two months*

* Bonuses are net of all charges except for the fixed investment management fee
** Annualised

### Asset Allocation

The strategic asset allocation of the bonus generating portfolio is shown alongside.




For more information on the bonus generating portfolio, Momentum MoM Enhanced Factor 7, please refer to our website: https://www.momentum.co.za/for/business/products/funds-at-work/fund-fact-sheets

For bonus declarations, 80% of the underlying assets returns of the bonus generating portfolio are smoothed over a three-year period as per the smoothing formula. The liability driven investment strategy includes a dynamic protection overlay to secure the guarantee.

As a result, for disinvestments other than guaranteed benefit payments the underlying assets value is sensitive to both asset values and interest rates and the effective asset allocation will reflect both the bonus generating portfolio and the dynamic protection overlay.

### Bonuses to be declared

Given that the monthly bonuses are based on the weighted average of the previous 36 months' returns of the bonus generating portfolio, it is possible to calculate the future bonuses that will be declared under various future investment return assumptions. Assuming zero returns over the following 36 months, around 8.15% of bonuses will still be declared. For a traditional smooth bonus product, this equates to a funding level between 102.5% - 107.5%.

Prior to the introduction of **the compass**, position, destination, and direction at sea were primarily determined by the sighting of landmarks, supplemented with the observation of the position of celestial bodies. On cloudy days, even the Vikings were at a loss for which way to go.

Because the compass is used for calculating heading, it provides a much improved navigational capability. And on our compass, security is the number one moral imperative.

# Smooth Bonus Products Key Features

| | | Fund Return Objective | Manager | Mandate Type | Guarantee on Benefit Payments[1] | Market Value Adjustment on Voluntary Exits[2] | Risk Charge | Investment Management Fee | Inception Date |
|---|---|---|---|---|---|---|---|---|---|
| Partially Vesting | Multi-Manager Smooth Growth Fund Global | CPI + 4% pa, net of charges over a 5 year time horizon | Multi-Manager | Moderate Balanced | 100% of capital invested and vested bonus declared | Yes | 1.00% pa | 0.60% of the first R50m, 0.50% of the excess above R50m[3] | January 2004 |
| Partially Vesting | Multi-Manager Smooth Growth Fund Local | CPI + 4% pa, net of charges over a 5 year time horizon | Multi-Manager | Moderate Balanced | 100% of capital invested and vested bonus declared | Yes | 1.00% pa | 0.55% of the first R50m, 0.45% of the excess above R50m[3] | January 2004 |
| Partially Vesting | Smooth Growth Fund Global | CPI + 4% pa, net of charges over the long to medium term | Momentum Asset Managers | Moderate Balanced | 100% of capital invested and vested bonus declared | Yes | 1.00% pa | 0.45% of the first R10m, 0.35% of the next R40m, 0.25% of the excess above R50m[3] | January 1989 |
| Fully Vesting | Multi-Manager Secure Growth Fund | CPI + 2% pa, net of charges over a 5 year time horizon | Multi-Manager | Moderate Conservative Balanced | 100% of capital invested and total bonus declared | Yes | 1.50% pa | 0.60% of the first R50m, 0.50% of the excess above R50m[3] | November 2007 |
| Fully Vesting | Multi-Manager Secure Growth Fund Bonus Series 2013 | CPI + 2% pa, net of charges over a 5 year time horizon | Multi-Manager | Moderate Conservative Balanced | 100% of capital invested and total bonus declared | Yes | 1.50% pa | 0.60% of the first R50m, 0.50% of the excess above R50m[3] | June 2013 |
| Fully Vesting | Capital Plus Fund | CPI + 3% pa, net of fees over a rolling 3 year period | Rand Merchant Bank | Structured Alternative | 100% of capital invested and total bonus declared | No | 0.50% pa[4] | | March 2005 |
| Fully Vesting | Smart Guarantee +3 Fund | CPI + 3% pa, net of fees over a 7 year time horizon | Multi-Manager Liability Driven Investment by Structured Solutions | Moderate Balanced | 100% of capital invested and total bonus declared | Yes | 0.50% pa | 0.90% pa[3] | October 2013 |

1. Benefit payments generally refer to resignation, retirement, death, disability and retrenchment. Specific benefit payments and terms and conditions are specified in client policy contracts.
2. Market value adjustments are applied if a client is underfunded
3. Depending on the underlying mandates that are negotiated with asset managers, net unit priced fees are and performance fees may deducted from the underlying assets
4. A performance fee of 25% of the outperformance above CPI + 2% p.a. + VAT is deducted from the underlying assets. The performance fee is capped at a maximum of 3% p.a. + VAT

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**Website:** www.momentum.co.za

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