ALLAN GRAY

QUARTERLY COMMENTARY 1

31 MARCH 2014

LONG-TERM THINKING IN ACTION

The cover of this Quarterly Commentary features the Tower of Hercules. This ancient Roman structure has stood tall on Spain's North Atlantic Coast for some 2 000 years and is considered to be the world's oldest lighthouse. Neither the rapidly changing world around it, nor the sea wildly lapping at the ground on which it stands, can shake its foundations. Remarkably, it is still used for its intended purpose: to guide ships through the treacherous ocean. The Tower of Hercules represents the investment philosophy that has guided us over the last 40 years. It is a tried and tested approach that allows us to invest with conviction, regardless of market conditions.

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ROB DOWER

COMMENTS FROM THE CHIEF OPERATING OFFICER

Adding value through stock picking, here and abroad

As you are most probably aware, asset allocation funds have the mandate to vary their exposure to asset classes, however our local Equity Fund and the Orbis Global Equity Fund are mandated to invest only in equities. Value-add in these funds comes only from the fund managers' stock-picking success.

Bearing in mind that the South African market is highly concentrated, the shares we own, as well as those we don't, have a big impact on our Equity Fund's performance. The top 10 holdings as listed on our fund factsheets give you an idea of our large holdings, but there are some small and mid-cap companies that make a significant difference to clients' returns. Although it is hard to make a case that generally small- and mid-cap shares are cheap in South Africa right now, the universe of such stocks is large enough that there are compelling investment opportunities among them available to diligent investors and analysts. Ian Liddle and analysts from his team provide an overview of some of the Fund's current small- and mid-cap holdings.

Living in South Africa, we are tempted to think that SA investments should make up the majority of our assets. It makes better sense to invest in the best opportunities in the world, and since SA makes up a small part of the world, it would be surprising if the majority of the best investment opportunities happened to be here.

The Orbis team has a much broader range of shares at its disposal. Investment analysts scour the global landscape for stocks that are trading at attractive multiples relative to their assessment of their true value, with little regard for the region or sector in which they are based. They often find opportunities when other market participants are fleeing, taking advantage of our shared long-term perspective and a willingness to see things differently.

It is unsurprising that the Orbis Global Equity Fund has a reasonable exposure to Asia, excluding Japan, which was a standout laggard in 2013. Like Allan Gray, Orbis makes investment decisions based on an assessment of the intrinsic value of individual stocks, not on overall geographies. However, with 7% of the Orbis Global Equity Fund invested in Chinese stocks, clients are asking about Orbis' view on the country's economy. Seema Dala highlights the trends that appear to be problematic, and outlines how Orbis has incorporated these into its bottom-up approach. She also discusses some of the attractive opportunities Orbis has found in developed markets, despite valuations looking stretched overall.

Global economics

Sandy McGregor draws a parallel between the outbreak of World War One in 1914 and the recent global financial crisis, arguing that the seeds for both lay in their preceding long periods of stability. Around the world, governments and policy makers attempt to engineer steady economic growth and stable price levels and exchange rates. This is fine, up to a point, but long periods of economic stability are ultimately self-defeating. Since market stability encourages increasing risk-taking, it ultimately causes instability. After a great period for global and SA stock markets, Sandy McGregor's piece offers a good reminder: long periods of stability can come to an end suddenly and in a way which is totally surprising.

Making better financial decisions

Asset allocation and fund selection are big decisions, and it's important to consider your investment objectives and the level of risk you can stomach before you commit to anything. If you are not comfortable making these decisions on your own, it is worthwhile consulting an independent financial adviser (IFA). Jeanette Marais discusses some of the merits of getting financial advice and offers a few practical points to consider when choosing an IFA.

If you want to be involved in the decision-making process, or if you wish to make your investment decisions unaided, it helps to know what to look for when picking a fund manager. With 1 477 registered unit trusts available locally, it's easy to become overwhelmed. Daniel van Andel offers a basic guide to picking a fund manager, and cautions investors against making a decision based on a single factor, such as the size of a fund.

It's also important to understand how a fund works so that you have some idea of what to expect from its performance. For example, you need to expect, and be able to stomach, short-term volatility from an equity fund. This will help you to remain invested for long enough to benefit from your fund manager's expertise, rather than 'switching' in a temporary dip. In this month's Investing Tutorial, Thandi Ngwane explains what switching is and why this should be a carefully considered investment decision.

I hope you enjoy this issue and look forward to your feedback. Thank you sincerely for your continued support.

Kind regards

Rob Dower

SANDY McGREGOR

THE STABILITY CONUNDRUM

The events which triggered World War One are a warning of the fragility of the global political system and economy. Looking at the current levels of global markets, Sandy McGregor cautions against complacency, as history suggests stability can come to an end in a way which is totally surprising.

The lessons of 1914

This year is the centenary of the outbreak of World War One, an anniversary which has prompted the publication of numerous books and articles on what caused this momentous event which so decisively changed modern history. For the past 100 years there has been a sense of astonishment that a seemingly unimportant incident, the assassination of the heir to the thrones of Austria-Hungary by a Bosnian revolutionary, could have such profound consequences, and could trigger a chain of events which resulted in a world war. Austria declared war on Serbia, which it blamed for the assassination. Russia mobilised its army to support Serbia. Germany regarded this as an unacceptable threat and declared war on Russia and Russia's ally France. Germany's inflexible military planning required it to invade France through Belgium. Britain had a treaty with Belgium and joined the war against Germany. Within two weeks all the great European powers were at war.

The role of chance and accident in these events was remarkable. For example, the assassin, Gavrilo Princip, was not standing on the chosen route for the Archduke's car. However, the Archduke's driver took a wrong turn and gave Princip the opportunity to carry out his purpose. So one can say that the consequences of a driver taking a wrong turn were the Great War, the overthrowing of the dynasties ruling Germany, Austria and Russia, the advent of Russian communism and, as a consequence of German defeat, the rise of Hitler who launched a second, even bigger war to reverse the decision of the first one. All because one driver made one mistake.

It also triggered a century of debate among historians about how this could have happened. How could a seemingly stable political order which had lasted 99 years following the end of the Napoleonic wars in 1815, suddenly implode? Perhaps the surreal character of these events is best evoked by the winning entry in a competition organised by a newspaper in the 1920s asking what would be the most sensational news headline. The winner was 'Archduke Franz Ferdinand alive. World War a mistake'.

Risk in an increasingly interconnected world

The events which triggered World War One are a warning of the fragility of the global political system and economy. One of the achievements of 20th century mathematics was to explain why we cannot successfully make long-range forecasts about the weather or the economy. Seemingly trivial and totally unpredictable events can have profound consequences, which make such predictions impossible. We now understand that if a butterfly flaps its wings in the Himalayas, it can trigger a hurricane in the Caribbean.

Complex systems tend to be less stable than simple ones. In an increasingly complex and interconnected global economy there is a growing danger that some totally unexpected event will have far-reaching adverse consequences. In recent years natural disasters such as the Fukushima tsunami in Japan, floods in Thailand and the Eyjafjallajökull volcanic eruption in Iceland, which disrupted air traffic in Europe, had adverse repercussions throughout the global supply chain. The great recessions of 1931 and 2008 were triggered by the failure of specific financial institutions (Credit Anstalt and Lehman Brothers), with consequences that cascaded through markets leaving few countries unaffected. History suggests that an economic system of ever-increasing complexity will inevitably become unstable.

"THE EVENTS WHICH TRIGGERED WORLD WAR ONE ARE A WARNING OF THE FRAGILITY OF THE GLOBAL POLITICAL SYSTEM AND ECONOMY."

The insights of Hyman Minsky

In the agendas of governments and policymakers, economic stability always ranks as a key objective. They regard stable currencies, stable price levels and stable exchange rates with approval. Above all, they want steady economic growth and abhor recessions. However, since market systems are inherently unstable, achieving these goals is extremely difficult. Some of the most important insights into this problem came from Hyman Minsky, an American economist who lived between 1919 and 1996. Minsky argued that stability creates instability. In financial markets long periods of stability promote ever-increasing risk taking, with market participants assuming increasingly extreme positions and taking on more and more debt. The longer the period of stability, the greater the financial excess and the more severe the inevitable correction. The conundrum governments face is that, in creating a stable economy, they ultimately generate a serious financial crisis. The most recent example of this was the implosion of the US housing bubble promoted by the Federal Reserve's success in creating a stable financial environment over a long period.

Minsky believed that the solution to this conundrum lies in substantially more regulation of financial markets, a view shared by many, and probably most, regulators. However, this approach does not solve the key problem that he identified, which is that stability ultimately causes instability. Another approach is to welcome greater market volatility, which would rapidly shut down excessive speculation. Unsustainable positions would be eliminated before they became big enough to threaten the stability of the system as a whole. Long-term stability requires an underlying instability to be sustainable.

The lessons of 1914 and of Minsky are the same. A long period of stability can come to an end suddenly and in a way which is totally surprising.

A time for caution

Investors are most complacent when they have been most successful. A long bull market breeds such complacency. We have now passed the fifth anniversary of the present bull market, which commenced in March 2009. In this period South Africa's FTSE/JSE All Share Index and the World Index denominated in dollars have both appreciated 135%. The actions of central banks have promoted a stable financial environment, which has allowed investors to make a lot of money. It is difficult to predict how and when the current financial boom will come to an end. However, the longer the upward movement in prices, the greater the risks of some unexpected event which brings what seems to be an inexorable bull market to a sudden end.

Sandy joined Allan Gray in October 1991. His current responsibilities include the management of fixed interest and individual client portfolios. Previously he was employed by Gold Fields of South Africa Limited for 22 years where much of his experience was focused on investment-related activities.

LEONARD KRÜGER

IAN LIDDLE

BIRTE SCHNEIDER

VICTOR SEANIE

RUAN STANDER

DIAMONDS IN THE ROUGH

Small- and mid-cap companies make up 16% of the FTSE/JSE All Share Index, but 25-30% of our clients' South African equity holdings. Although many of these shares are currently too small to be included in our top 10 holdings, they can still contribute significantly to our clients' investment returns. We exert considerable research effort on small- and mid-cap opportunities. Ian Liddle and analysts from his team provide an overview of some of our funds' current small- and mid-cap holdings.

On a superficial inspection, South African small- and mid-cap shares currently offer marginally better value than the top 40 large capitalisation companies, as shown in **Table 1**. However, they certainly do not appear to be offering the same very attractive relative value that they were in 2001/2. After rebounding strongly from their lows in 2001/2, small- and mid-cap shares have performed broadly in line with the top 40 over the last nine years. See **Graph 1** on page 6 and **Graph 2** on page 7.

While these aggregate measures provide useful context, we do not use them to determine the current allocation of roughly 25-30% of our South African equity portfolios to small- and mid-cap stocks. Each small- or mid-cap share in our portfolios has been bought by an individually accountable portfolio manager after the share has passed through our research process.

While these shares may never make our top 10 holdings list by virtue of their small size, any one of them may have a significant impact on our equity alpha (performance relative to the benchmark) if it appreciates substantially. Of course, their collective impact could be even larger. We thus exert considerable research effort in searching for these 'diamonds in the rough'.

To give you a flavour of some of the opportunities we are currently identifying, each responsible analyst has written a brief synopsis of some of our current small-cap holdings.

Adcorp (Analyst: Birte Schneider)

Adcorp is South Africa's largest employment services group. The risk of a labour broking ban has been significantly reduced, although stricter regulation of casual labour hire practices is likely. The increasing administrative and regulatory burden and a global shift to master service providers favour large, sophisticated players with strong balance sheets, such as Adcorp. In addition to market share gains, economic and labour market uncertainty supports its South African business.

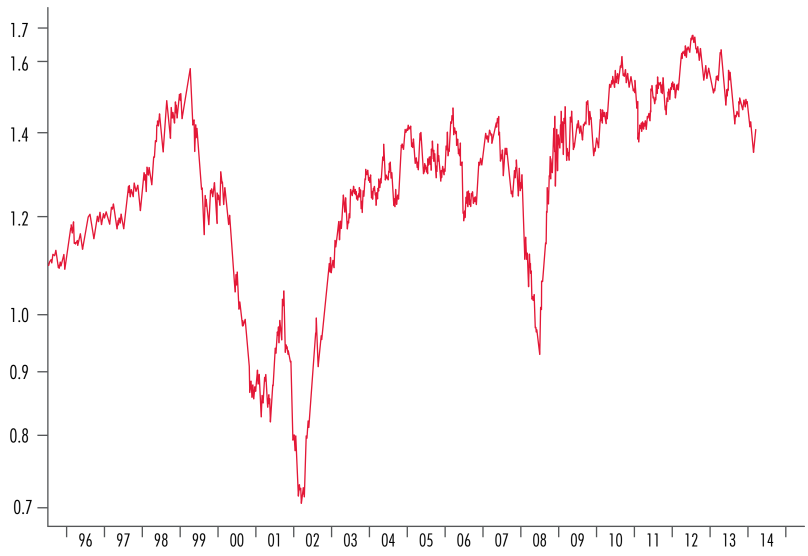
In recent years, Adcorp diversified its earnings stream through organic growth and acquisitions at reasonable

TABLE 1 **A COMPARISON OF EARNINGS AND DIVIDEND YIELDS**

	TOP 40	MID-CAP	SMALL-CAP
Earnings yield	5.7%	6.4%	7.4%
Dividend yield	2.7%	3.1%	3.8%

Sources: FTSE/JSE Indices, I-Net Bridge

GRAPH 1 **RATIO OF MID-CAP INDEX DIVIDED BY TOP 40 INDEX**



Source: I-Net Bridge

valuations, particularly in the IT contracting sector. It now has operations in Africa, Australia and India. For the six months to August 2013, 21% of earnings before interest, tax, depreciation and amortisation (EBITDA) was generated outside South Africa, compared to 3% a year earlier. This segment is positioned for strong growth. Further upside potential is provided by its business process outsourcing and training operations, cost savings from outsourcing back office functions and taxation deductions for learnerships. The company is cash generative and trades at only 8.5x normalised earnings.

Blue Label Telecoms (Analyst: Victor Seanie)

With over 150 000 point of sale (POS) payment terminals, Blue Label Telecoms is South Africa's largest distributor of prepaid airtime and electricity. Its prepaid airtime distribution market share is approximately 40%, and the number of existing POS distribution points through which electricity is sold is expanding. It continues to add new prepaid products such as transport, sport and entertainment tickets and financial services to its distribution basket, with little additional capital investment.

Through its 45%-owned associate, Blue Label Mexico (68 000 POS terminals installed so far), Blue Label Telecoms is currently investing in POS terminals to replicate its South African prepaid product distribution model in Mexico. Similarly, the company is expanding its 130 000 POS terminal base in India and rolling out banking services to the unbanked.

The group is led by an entrepreneurial management team with a significant shareholding in the business. The company is trading on a price to earnings (PE) multiple of 13 on earnings that include start-up losses in Mexico.

"SMALL- AND MID-CAP COMPANIES MAKE UP 16% OF THE FTSE/JSE ALL SHARE INDEX, BUT 25-30% OF OUR CLIENTS' SOUTH AFRICAN EQUITY HOLDINGS."

Clover (Analyst: Leonard Krüger)

Clover is truly a household name and chances are that one of its products is in your fridge at this very moment. Yet the company faced deep issues prior to 2010 as milk farming moved steadily to the coastal regions over the years, away from Clover's factories. This resulted in big cost pressures, as fuel prices increased and driving distances became ever greater.

Under project 'Blue Sky', the business has rectified these challenges and added capacity to deliver a wider range of products in future using its extensive distribution network.
One such opportunity is yoghurt. Previously excluded from this product for historical reasons, Clover will re-enter the yoghurt market in 2015. Added to its portfolio, together with many other new innovative and chilled products, we believe Clover's margins and returns are still low for a business of this quality. At 13x historic earnings, in our opinion the long-term revenue and profit growth opportunity is not reflected in the share price.

Comair (Analyst: Leonard Krüger)

Airlines operate in a notoriously difficult industry as the number of domestic bankruptcies over the past decade would testify. Yet, despite fluctuating oil prices and a volatile rand exchange rate, Comair has built an enviable track record of unbroken profitability for over 60 years.

This has allowed the airline to continue investing in more fuel-efficient aeroplanes, to lead in local industry

GRAPH 2 **RATIO OF SMALL-CAP INDEX DIVIDED BY TOP 40 INDEX**

Source: I-Net Bridge

innovation (e.g. low-cost carrier kulula.com) and to implement enhanced information technology. With smarter and slicker systems, Comair today is better able to manage its inventory of unsold seats, increase revenue by selling more services like extra baggage or insurance, and potentially acting as a platform for other airlines to sell seats in South Africa (such as British Airways).

These investments place Comair at a substantial advantage over state-owned rival SAA and any would-be new entrant, by having lower operating costs and greater efficiency in management. The current PE multiple of 6x neither properly recognises the sustainability of this advantage, nor Comair's opportunity to make further improvements. It also ignores the potential for Comair to succeed in the various legal claims it has against SAA for uncompetitive practices.

KAP (Analyst: Ruan Stander)

At R3.75 for a KAP share, the market offers a top-quality industrial holding company on a 6.7% free cash flow yield, with free cash flow expected to grow strongly over the next 10 years. KAP's major holdings include Unitrans, PG Bison and Hosaf.

Supply chain and logistics solutions provider Unitrans has a great track record of growing profitably by offering reliable service in areas where it is critical. Who would want to save 1% on moving petroleum when everyone knows Unitrans does it safely?

PG Bison, South Africa's leading timber company, is fresh out of a successful restructuring that focuses the group on the most profitable areas in the timber value chain. The savings from these actions have been re-invested into new technology, the benefits of which will be seen for the first time in the next results.

Hosaf is the country's only manufacturer of PET, the key ingredient used in plastic bottles. A growing market for plastic bottles offers attractive growth opportunities to this business.

Net1 UEPS Technologies (Analyst: Ian Liddle)

Since winning the national tender for the distribution of social grants, Net1 has registered nearly 22 million social grant beneficiaries and recorded their biometric data. The company is now responsible for paying over R9 billion rand every month to grant recipients on behalf of the South African government. Grant recipients are able to draw this monthly grant from Net1's cash payment points in rural areas, ATMs or from POS machines in retail stores. Net1's biometric verification technologies are already resulting in substantial savings for the government through reduction of fraud. These savings could amount to billions of rands per year. Although the company will have to re-tender for the national contract within the next four years, it will have a substantial competitive advantage over any potential competitor. Net1 is developing a formidable track record of successfully implementing reliable and robust technology, which comfortably handles millions of transactions, both on- and offline. Any new provider would have to make substantial investments in setup costs, which are now behind Net1.

"WE EXERT CONSIDERABLE RESEARCH EFFORT IN SEARCHING FOR THESE 'DIAMONDS IN THE ROUGH'."

Why is the share trading for just 7x forward earnings? The losing bidder in the national tender process (an Absa subsidiary) has challenged the outcome of the tender through the courts all the way to the Constitutional Court. Different judges have made conflicting rulings as the matter has progressed. This creates considerable uncertainty. It is possible that the Constitutional Court will make an extremely adverse ruling for Net1 (a final ruling is still outstanding at the time of writing), in which case the share will be a disappointing investment. But on a balance of probabilities (taking into account the vital role Net1 performs in distributing cash to needy South Africans), we believe Net1 is attractively priced. The risk of an adverse ruling is mitigated by limiting the position size in our clients' portfolios.

Leonard is a qualified actuary. He joined Allan Gray in July 2007 and is a member of the investment team.

Ian is our chief investment officer, with overall responsibility for the investment team and portfolio management. He joined Allan Gray in 2001 after several years as a management consultant. He is a director of Allan Gray Proprietary Limited and a CFA charter holder.

Birte joined Allan Gray as an investment analyst in 2011. She has an MPhil in Finance from the University of Cambridge and is a CA(SA).

Victor joined Allan Gray as an equity analyst in 2009. He has a Bachelors of Business Science, with Honours in Finance. He is a CA(SA) and CFA charter holder.

Ruan joined Allan Gray in 2008. He is a quantitative and equity analyst, associate portfolio manager in our equity and balanced portfolios, and portfolio manager of the Allan Gray Optimal Fund. He has an Honours Degree in Financial and Actuarial Mathematics and is a certified GARP Financial Risk Manager.

SEEMA DALA

FINDING VALUE IN GLOBAL MARKETS

Emerging markets have come under intense focus so far this year and while the main worries have centred on countries such as Argentina and Turkey, the market wobbles in 2014 have refocused attention on the health or otherwise of the Chinese economy. As a bottom-up stock picker, Orbis does not invest based on a top-down macro view. However, as 7% of the Orbis Global Equity Fund is invested in Chinese stocks, it is not surprising that clients have been asking about Orbis' view on the country's economy. Seema Dala highlights the trends that appear to be increasingly problematic, and outlines how Orbis has incorporated these into its bottom-up approach. She also discusses some opportunities Orbis has found in developed markets, despite valuations looking stretched overall.

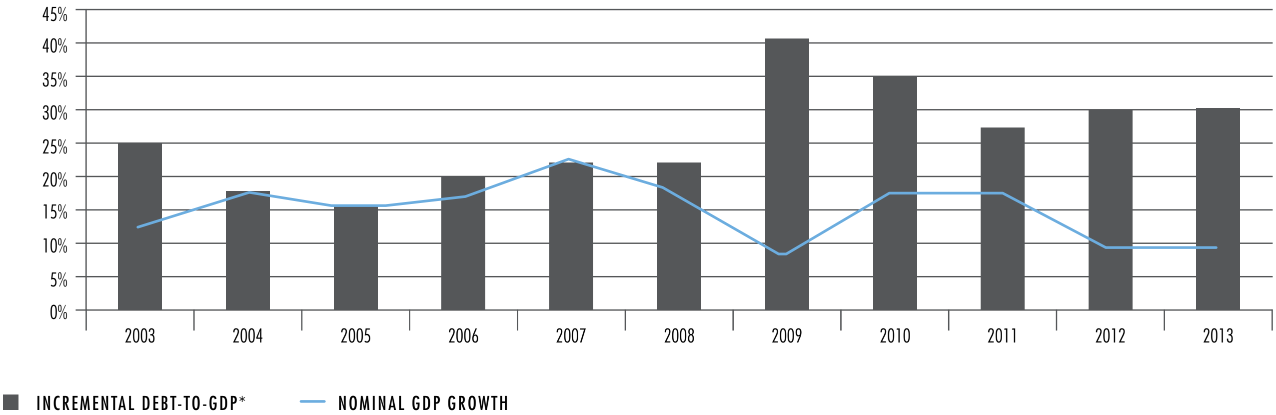
Economists tend to look at credit growth as a key predictor of future financial instability. Throughout history, excessive credit growth and an accompanying property bubble have often been followed by an economic bust. Because of this, Orbis is mindful that some of the conditions that preceded the world's recent financial crises resemble the current environment in China.

Since the November 2008 stimulus package designed to mitigate the shock of the global financial crisis, China's outstanding total social financing (TSF), an approximate measure of the country's debt, has expanded at a compound annual growth rate of about 23%. As a result, China's debt-to-GDP ratio soared from 130% in 2008 to about 200% in 2013. The scale of this expansion outstrips that experienced by either Japan in the late 1980s or the US in the years before 2008. This is of increasing concern given the deceleration in underlying economic activities as measured by indicators including retail sales, Purchasing Managers Index, power generation, railway cargo volumes, port cargo throughput and GDP growth, the latter of which is shown in **Graph 1**.

Despite ballooning credit, many parts of the real economy have suffered from difficulty in accessing bank loans and rising interest costs, while overcapacity issues have worsened in many capital-intensive industries. Indeed, the Producer Price Index, a measure of the prices of goods as they leave the factory, slipped from 1.7% in 2011 to -1.9% in 2012 and -1.4% in 2013. One explanation for all this is that a large portion of capital invested in China has been misallocated to projects with poor returns and cash flows, such as infrastructure and oversupplied industries. These projects are frequently state-owned or 'too-big-to-fail' yet continue to access financing under China's state-owned banking system. As these 'zombie' projects continue to absorb the credit supply, the provision of credit to other parts of the economy has become crowded out, forcing more financially healthy private enterprises to pay higher rates of interest.

"...SOME OF THE BEST OPPORTUNITIES ARISE WHENEVER FEAR OR UNCERTAINTY GIVE RISE TO SHORT-TERM THINKING OR FORCED SELLING..."

GRAPH 1 CHINA'S DEBT CONTINUES TO INCREASE WHILE OUTPUT GROWTH IS FALLING



*Incremental debt-to-GDP is defined as incremental total social financing to nominal GDP.

Source: Orbis

Exacerbating the emerging credit bubble is the duration mismatch between assets and liabilities. On the asset side, an increasing portion of credit has been plunged into very long-term assets, such as infrastructure, property and industrial capacity. However, as shown in **Graph 2**, financing for this has come increasingly from the shadow banking sector in the form of trust loans, bank acceptances and entrusted loans, which can have short durations and unsteady flows. These shadow banking products are financed in turn by funds with shorter durations, such as interbank lending, which can be callable in as little as one month.

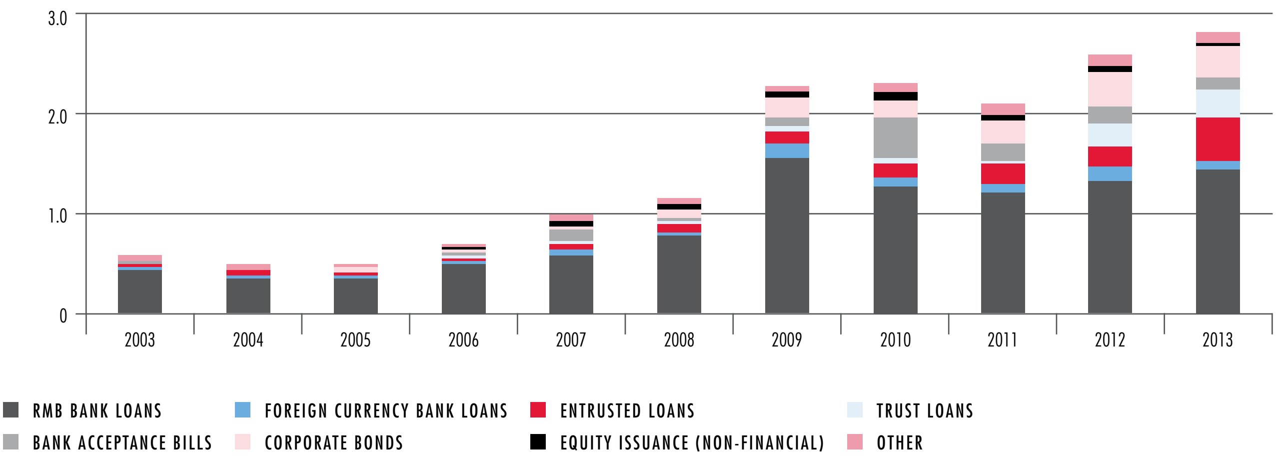
So far, different parts of the Chinese government have allowed the debt binge to continue by bailing out many potential defaults. However, Orbis worries that the scale of non-performing debt might become too great to be bailed out and defaults will surge.

So why invest in Chinese stocks at all?

To answer this question, it is important to remember that Orbis invests clients' capital in shares they think are undervalued irrespective of developments in an economy, and strives to avoid companies that derive meaningful profits from unsustainable activities and depend on short-term funding. For these reasons Orbis has found few shares in certain sectors, such as banks, property developers, miners and investment-driven stocks. However, the Chinese market is diverse and Orbis has found appealing stocks in other areas, such as the technology sector.

Over half of the Orbis Global Equity Fund's Chinese exposure is allocated to two names, Sohu.com and NetEase, both of which have very strong balance sheets and derive the majority of their earnings from consumers' desire to play online games. They are

GRAPH 2 BREAKDOWN OF CHINA'S INCREMENTAL TOTAL SOCIAL FINANCING IN BILLIONS OF US$



Source: Orbis

also geared to the secular growth of Chinese internet usage – a trend Orbis believes is largely independent of their concerns with the Chinese economy. Orbis does not believe the market has priced in their long-term growth potential.

Opportunities in the developed world

By contrast, many developed market valuations are looking stretched. Despite this, there are some sectors where Orbis believes the stock market is overly pessimistic about short-term developments. The media sector, for example, is a cyclical industry where the future is likely to resemble the past and the markets' concerns may be resolved in the fullness of time. Orbis currently owns a selection of media shares, in particular cable companies, which together account for 9% of the Fund.

Cable companies stand out as owners of high-quality assets because in many markets they have a monopoly for high-speed broadband, which has increasingly become a 'must-have' service. With broadband penetration in the US and Europe still only in the 30-40% range of potential customers, Orbis believes cable has considerable room for future growth, and cable stocks have been mispriced. Naysayers often point to the trend of 'cord cutting', in which customers cancel their cable video subscriptions in favour of online services such as Netflix. Orbis believes this concern is overdone for a few reasons. First, even though Netflix has more than 30 million subscribers in the US – and many more in reality through widespread password sharing – video subscriber losses at US cable companies have been relatively limited, supporting Orbis' view that these services are being used to complement, rather than to replace, cable. Second, Orbis believes traditional cable continues to offer tremendous value to most consumers.

The Fund also stands to benefit from specific factors unique to each company. Charter Communications, for example, can be considered a 'turnaround thesis' in which Orbis expects the future to be very different from the past. Under previous management, the company had underperformed its peers on most operating metrics, but it is now being run by a team of proven cable operators. Meanwhile, Charter's largest shareholder, John Malone, is arguably the industry's best deal-maker and capital allocator. Orbis expects capital spending to normalise after Charter completes its roll-out of new, all-digital equipment. At that point, they expect that the company will be able to earn about US$14 in free cash flow per share. At the current share price, this means that the business yields a more than 11% per annum stream of cash that the company can reinvest or return to shareholders.

A second example in the Fund is Liberty Global, which is a 'consolidation thesis'. Controlled by Malone, Liberty's shares are listed in the US but nearly all of its operations are in Europe. Liberty is steadily gaining market share and subscribers in some of Europe's largest markets. This comes as little surprise to Orbis, as Malone pursued a similar strategy in the US. Orbis established its position last year at an attractive price when the stock was under heavy selling pressure from investors seeking to hedge their exposure to Virgin Media, a UK cable provider that was bought by Liberty. Orbis recently had a similar opportunity to add more shares after the announcement of Liberty's acquisition of Ziggo, a leading Dutch cable company.

In both situations, the market did not give Liberty enough credit for the attractive price being paid and the synergies resulting from consolidation and capital structure changes.
As the dust settles from Liberty's recent acquisitions and synergies are realised, Orbis estimates that the company can earn US$4.50 in free cash flow per share – a more than 10% yield to reinvest or return to shareholders. Orbis finds this particularly attractive considering that Liberty's cash flow can continue to grow steadily at a high single-digit rate as more subscribers are added and there is potentially further upside from shareholder-friendly capital allocation decisions.

Long-term outlook gives perspective

Only time will tell how global stock markets will fare in the year ahead. Every investment environment has a set of risks, and this one is no different. Orbis' experience has shown that some of the best opportunities arise whenever fear or uncertainty give rise to short-term thinking or forced selling on the part of other market participants. As always, Orbis seeks to take advantage of both their long-term perspective and a willingness to see things differently – an approach that has served Orbis well through a wide range of market environments.

Seema is a member of the Institutional Client Servicing team and is responsible for Orbis client servicing in South Africa. She joined Allan Gray in 2007 as an investment analyst and is a qualified CA(SA).

JEANETTE MARAIS

WHAT ARE THE MERITS OF GOOD, INDEPENDENT ADVICE?

Many investors lack the time, knowledge and experience to invest successfully, often encountering difficulties that could have been avoided had they taken advice from an independent financial adviser (IFA) at the outset and continued to listen to their counsel over time. Jeanette Marais discusses some of the merits of getting financial advice and offers a few practical points to consider when choosing an IFA.

I recently overheard a financial adviser tell a client: 'I am not here to make you a lot of money. If you want someone to do that, and trade shares back and forth, then I'm not the person; but if you're looking for someone who makes investments consistent with your risk tolerance and goals, then I can help you.' This got me thinking about how many people have misconceptions about the role IFAs play. While not every investor may need, want or be able to afford an adviser, it is worthwhile understanding that IFAs are more than just product pickers; they play an important role in helping you make decisions that are right for your circumstances and, importantly, help you to avoid the pitfalls of investing on your own (see **text box** on page 14).

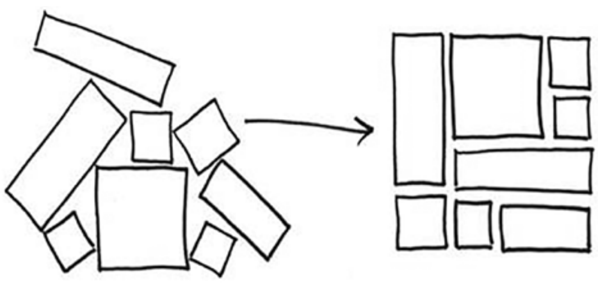
The role of a financial adviser

The critical starting point for achieving financial freedom is a well-crafted financial plan. This should document your financial goals and serve as the point of departure for making informed decisions that suit your unique circumstances. While you can naturally put a plan in place yourself, an adviser will help you to figure out the complexities of your financial situation, identify potential gaps in your thinking, and help formalise your plan based on your attitude towards risk, your time frame for results and your personal priorities.

Once your plan is in place, an IFA will help you to navigate the investment options available and ensure that you make the right choices based on your goals and circumstances. Financial adviser and New York Times blogger Carl Richards sums it up well in his sketch below: financial advice brings order to chaos.

You can also rely on your adviser to stay abreast of investment trends and changes in regulations, tax and product offerings. Your adviser will review your situation regularly, report

SKETCH **FINANCIAL ADVICE BRINGS ORDER TO CHAOS**



Source: Carl Richards, Behaviorgap.com

back to you and revise your plan as necessary so that you can stay on track to meet your goals.

There are a number of less obvious benefits to having an IFA. An adviser serves as a 'voice of reason', minimising doubt in volatile times, helping you to be rational rather than emotional about your investments, and encouraging you to avoid switching between investments for the wrong reasons. An adviser will ensure that a disciplined savings and investment process is implemented and maintained, thus eliminating any tendency to procrastinate and allowing you to gain valuable time in the market.

> **"AN ADVISER SERVES AS A 'VOICE OF REASON', MINIMISING DOUBT IN VOLATILE TIMES, HELPING YOU TO BE RATIONAL RATHER THAN EMOTIONAL ABOUT YOUR INVESTMENTS..."**

Important considerations when selecting an adviser

Your IFA will advise you on some of the most important decisions in your life, so your choice should not be taken lightly. Some points to consider:

1. **Trust**

A good relationship with an adviser is founded on trust. You need to know that s/he is honest, values your business and has your best interests at heart.

2. **Credentials and qualifications**

By law, all financial advisers must be licensed by the Financial Services Board (FSB). To get a license, they need to pass regulatory exams and fulfil the FSB's Fit and Proper requirements (including honesty, integrity and competency). All advisers must prove to the FSB on an ongoing basis that they are developing and maintaining their professional competence. To add an additional layer of reassurance, at Allan Gray we also perform regular credit reference checks on IFAs who have contracts with us.

Apart from these basics, you should question prospective advisers about their academic or other credentials.

3. **Your rights**

Financial advice and those who provide it are strictly regulated. If you believe that you been misled, have not received appropriate advice, or have been unfairly charged, you should raise your concerns with your adviser.

If you have a complaint which cannot be resolved, you can turn to the Office of the Ombud for Financial Services Providers, referred to as the FAIS Ombud, for help.

4. **The importance of independence**

The best advice is independent advice. A proper Independent Financial Adviser is not incentivised to advise on some products over others or employed by product providers to sell their products. S/he is not restricted to selling the products of any one company. In addition, there are laws in place that aim to prevent conflicts of interest between independent advisers and product providers, which means a higher likelihood that an independent adviser will remain objective and choose the products that are best suited to you.

5. **Fees**

Disclosure and transparency are crucial – make sure that your adviser explains to you upfront what fees you will pay and how they work.

Fees are usually charged as a percentage of the value of your investment. The product provider will deduct the amount from your investment and pay it over to the adviser on your behalf, i.e. it will be deducted from your investment total. These fees cannot be charged or paid unless you have agreed to them. Fees of this nature include initial and annual (ongoing) fees. An initial fee is based on the value of your investment and will be deducted from the initial sum invested, and paid to the adviser. An annual fee is based on the value of your investment, but it is calculated daily to allow for any fluctuation in your investment's value over the year.

Allan Gray has set parameters of 0% to 1% on annual fees, but will only allow an adviser to charge a maximum annual fee of 0.5% if he has charged an initial fee that exceeds 1.5%. Where the annual fee exceeds 0.5%, the initial fee will be limited to 1.5%. The fee parameter for initial fees is between 0% and 3%. Allan Gray has initiated these parameters as we feel that they are fair and reasonable caps on rates that clients should pay for advice.

Some financial advisers use a different fee model entirely, charging for the advice provided directly, as a rand amount, usually an hourly rate.

At Allan Gray we do not pay commission as we believe that products with built-in commission have the potential to skew an adviser's preference and therefore prevent him from being able to offer properly independent advice.

Finding an adviser

Bearing in mind that a key consideration in selecting an adviser is trust, a good starting point in looking for an adviser is to ask for a recommendation from someone whose judgment you value. You could also turn to the Financial Planning Institute of Southern Africa (FPI) for help.

Some companies provide the contact details of trusted IFAs on their websites, such as Allan Gray's 'Find an adviser', which can be found under the 'Quick links' menu on our homepage www.allangray.co.za. All advisers listed have been recommended by their clients.

Do you need financial advice?

Allan Gray does not offer advice but we do believe in the merits of independent investment advice for those who lack the knowledge and skill to make investment decisions unaided. If you are not comfortable making your own investment decisions, or do not have the time, we suggest you engage the services of an independent financial adviser.

If you cannot afford good advice, or if you feel equipped to make your own financial decisions, it remains your prerogative to choose how to invest with Allan Gray.

How a financial adviser can assist

An adviser can help you avoid some typical mistakes investors make, such as:

1. **Investing without a plan**
   If you do not know where you are going, how will you know when you get there? If you have some money to invest take the time to consider your goals and needs. Do you need to save for your child's education? Do you need retirement savings? A financial adviser can help you think things through and develop a workable plan.

2. **Investing in the wrong product or fund**
   The choice of products and funds available is mind-boggling. Different products have different tax structures, while different funds have different objectives. An adviser can assist you in making choices suitable for your circumstances.

3. **Not thinking about inflation**
   Time can erode the value of your money, leaving you able to buy less with the same amount of rands. This is called inflation. The returns on your investment should be at least enough to compensate you for the length of time that you invest so that the value of your money is maintained. An adviser can help you to achieve this.

4. **'Blowing' your retirement savings when you change jobs**
   If you have been retrenched or are changing jobs, make sure you preserve the retirement savings you have built up. If you do not, you probably will not be able to retire with enough money to live on. An adviser can encourage you to preserve your savings.

5. **Focusing only on one market and one asset class**
   One of the keys to successful investing is diversification. In other words, do not have all your eggs in one basket. For example, in addition to South African investments, including offshore investments in your portfolio can help your savings grow, while lowering your risk. An adviser can help you to make sure your investments are adequately diversified.

6. **Acting on your emotions**
   Investors are particularly bad at picking the right times to buy or sell investments. In addition, they tend to switch between investments too often, destroying the value of their savings. An adviser will help you avoid this pitfall.

Jeanette jointly heads up the retail business. She is specifically responsible for client services and manages the different channels through which our clients access our retail products. She is a director of Allan Gray Investment Services Proprietary Limited and Allan Gray Unit Trust Management (RF) Proprietary Limited.

DANIEL VAN ANDEL

DOES THE SIZE OF YOUR UNIT TRUST MATTER?

Back in September 1998, there were 186 unit trusts available in South Africa. Fast-forward 16 years, and there are now 1 477 registered unit trusts in a variety of different investment strategies and styles to choose from. This makes the job of selecting the correct unit trust for an investment a tough task. Daniel van Andel discusses why you should not be too distracted by size, and offers a basic guide to picking a fund manager.

Something which advisers and investors are often unsure of, is how much consideration they should give to size when purchasing a fund. At R83 billion, the largest rand-denominated fund in the industry (the Allan Gray Balanced Fund) is around 80 000 times larger than the smallest start-up fund. To put this into perspective, visualise the difference in size between a fully grown adult elephant and a mouse! It is hardly surprising that many investors are left wondering what an impact this disparity in size has on the returns managers are able to generate. Is it important to consider size when selecting a unit trust or is it a distraction which should not be part of the decision-making process?

"WE WERE UNABLE TO UNCOVER ANY EVIDENCE OF A CORRELATION, EITHER POSITIVE OR NEGATIVE, BETWEEN THE SIZE OF A FUND AND THE PERFORMANCE IT WAS ABLE TO GENERATE."

In theory the size of the asset manager you choose can be a good and a bad thing

Let us continue with the analogy of the mouse and the elephant. The small, more agile mouse is able to change direction far more quickly than the larger, somewhat cumbersome, elephant. In the same way, smaller asset managers are able to quickly change the look of their portfolios, while larger asset managers are forced to adopt a longer-term approach when purchasing and selling positions. The mouse can also go where it chooses, easily allocating significant portions of a portfolio to the shares of any company. The elephant, on the other hand, is constrained by where it can go and inevitably leaves a trail behind it when forging a path. In the same way large asset managers are constrained to investing significant proportions of their portfolios in the shares of large companies and sometimes struggle to do so without impacting the price of these shares in the market.

Theory has it that large fund managers have more assets to invest and are thus forced to hold positions in shares which they would not necessarily have held, had the level of their assets under management been lower. What is important to remember, is that both the market capitalisation and the number of shares available for purchase on the stock exchange grow over time. Therefore, the level of assets managed and the number of shares a manager invests in, should be considered relative to what is available on the stock exchange and not in absolute terms.

Scale has its benefits. For example, scale should help asset managers remain in business and stick to their investment philosophies during prolonged periods of adverse market conditions that they have no control over – something that the small asset managers may not have the luxury of doing. Also, large asset managers have access to superior research which, if used correctly, could translate into stronger performance over the long term. To complicate matters further, large managers are not all large by virtue of good marketing or luck: some are large because they are skilled and have therefore delivered attractive returns and flows. Small managers are not all small deliberately because they enjoy the freedom of being nimble: this group includes some that have not shown evidence of skill and therefore failed to attract assets.

Size is relative

Considered next to a mouse, an elephant seems large. But an elephant has plenty of room to manoeuvre in the Kruger National Park. Even the largest funds in our unit trust universe are able to take quite different positions in their universe of potential investment. The JSE has a market capitalisation of R9 trillion, about 100 times bigger than the largest fund, which invests its assets in shares but also in bonds, cash and internationally. This is evident in the very differing performances of even the largest funds in our sample in **Graph 1**, and the fact that fund positions deviate from the index regardless of fund size.

Theory is one thing, but what of evidence?

We have not come across any compelling evidence of a correlation between performance and the level of assets under management in the South African market. This may seem surprising, but to test our theory we categorised all active unit trusts in South Africa's general equity sector by size and took a look at the one-, three- and five-year rolling returns which they were able to generate for the years 2006 to 2013. We were unable to uncover any evidence of a correlation, either positive or negative, between the size of a fund and the performance it was able to generate. Further, we were unable to uncover anything suggesting that the returns generated by large funds deviate less (and therefore conform more) compared with an appropriate benchmark relative to the returns generated by small funds.

These findings are in line with other research done on this topic* both in the South African market and elsewhere in the world, which concludes that the relationship between size and performance, in general, is neither positive nor negative, with certain years favouring large funds.

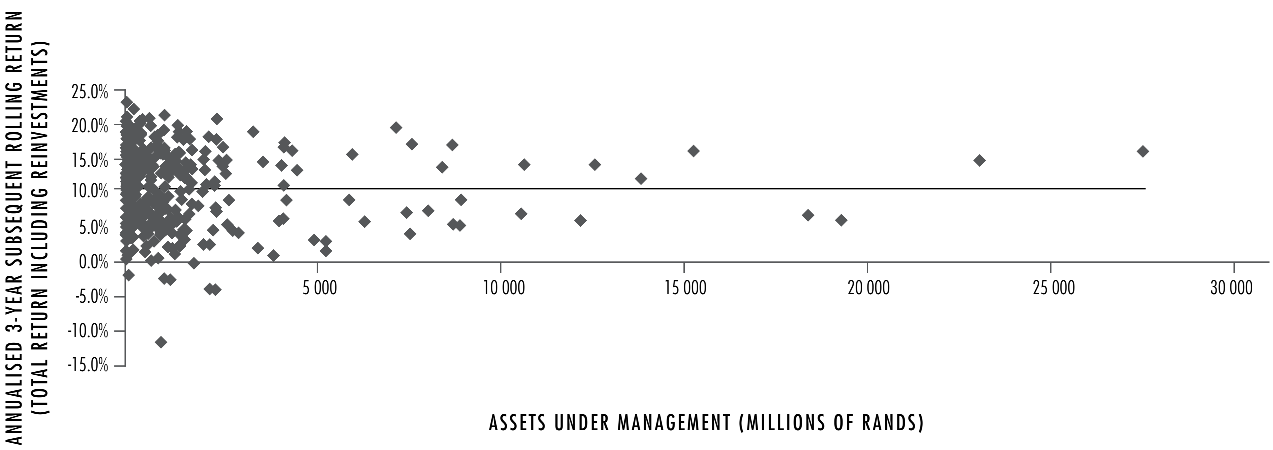
If size is not a concern, what should you focus on?

Here is a basic guide to picking a unit trust manager:

1. Identify management companies with a proven track record of long-term success. On average, fund managers underperform index benchmarks after management fees have been deducted: this must mathematically be so (assuming that the performance of the average fund manager is equal to the benchmark, it stands to reason that the average fund manager will underperform the benchmark once fees are taken into account). A surprisingly small number of managers outperform the ALSI, and over long periods this performance is more persistent than short periods.

2. Look for a management company that is able to attract and retain the best talent and that has a proven and consistently applied process and philosophy. These considerations are more likely to have a far greater impact on the

GRAPH 1 **NO CORRELATION BETWEEN PERFORMANCE AND ASSETS UNDER MANAGEMENT***



* The scatter plot shows the assets under management of each unit trust along with its subsequent three-year rolling return for the period 2006 - 2013.

Source: Allan Gray research

performance of your investment than the size of the unit trust you decide to invest in.

3. Make use of quality independent information available, such as evaluations which rating agencies perform on unit trusts available for investment in South Africa. Fundhouse, an independent qualitative fund ratings agency, has rated all the unit trusts available on Allan Gray's investment platform. To view these ratings, or for more information on the evaluation process and the three tiers which Fundhouse uses to categorise unit trusts, please refer to our local and offshore fund lists available on our website www.allangray.co.za

4. Do not switch around. Short-term switching tends to destroy value because it usually happens just after one fund has done badly and the other has done well (please see Thandi Ngwane's piece on page 18 to learn more about switching). Although past performance is not a predictor of future performance, identifying and investing with a manager that has a proven track record of long-term success should give you the confidence you need to stick with your choice when it lags competitors, and not switch.

5. Consider getting advice. Choosing the right manager is a complex task. If you do not feel comfortable making your own investment decisions you may wish to consult an independent financial adviser. (Please see Jeanette Marais' piece on page 12, which discusses the merits of good, independent advice).

* You can read Dave Bradfield's paper 'The latest on fund size – What insights are there for fund management?' and N Pillay, C Muller and M Ward's paper 'Fund size and returns on the JSE'.

Daniel joined Allan Gray in 2009 and is a business analyst in the product development team. He has a BCom (Hons) from the University of Stellenbosch and his CFA charter is pending the required years of work experience.

THANDI NGWANE

WHAT IS SWITCHING?

We often caution investors against 'switching' at the wrong moments. But what exactly is switching and how do you know whether or not it is an opportune time to switch? Thandi Ngwane explains.

Switching involves selling units in one unit trust to buy units in another. You can usually make a switch quite easily – at Allan Gray you can do this online or by filling in a form, and with no fees – but as with all investment decisions, you should carefully consider your actions.

Why do investors switch?

Investors are often tempted to switch between funds in an attempt to improve their returns. The fund they originally selected may be going through a period of relatively poor performance and they may sense a better opportunity elsewhere. Selling a unit trust that has performed poorly over a short period is often an emotional response, and emotional switching invariably destroys returns. When your investment has lost value can be the worst time to switch, as you land up locking in losses.

While some investors improve their returns by switching out of one fund and into another, research shows that more often than not switching destroys value. On average, investors earn lower returns than the funds in which they are invested. The point of a unit trust investment is to access the expertise of a skilled manager; your role as the investor is to select a unit trust with investment objectives aligned with your own and to stay invested for long enough to benefit from this expertise.

Some investors deliberately switch between good funds in an attempt to time the ups and downs of each fund's performance. Timing the market is extremely difficult to do successfully, because a large component of short-term returns is random and therefore inherently unpredictable. Regardless of motivation, active switching distracts investors from the important and difficult task of picking a good fund for long-term returns.

Counting the costs

Another reason to avoid switching between funds is that selling units may trigger capital gains tax (CGT). In addition, the fund you switch into may charge initial fees. These short-term costs may seem acceptable for an investor wanting to get into a new fund, but with frequent switches, CGT and other switching costs add up to a significant drag on long-term returns.

So when should you consider switching?

If you have an investment objective and have selected an appropriate unit trust you should usually only consider switching in response to a change in your objective. However, if you are concerned about your unit trust's performance, you need to do some research to check that you have not picked a poor quality fund or that your fund has not changed in some important way.

- All funds go through good and bad periods of performance. The best funds have more good periods than bad, and switching out of one of these during a bad period is normally a bad idea as you miss out on the good period that follows. On the other hand, sticking with a fund that perpetually underperforms is also a bad idea. The only way to distinguish between these two situations is to do your research.
- Look at your fund's performance in the context of its objectives. If, for example, you are invested in an equity fund which states that you need to expect volatile returns over the short term, then some loss of value should not concern you unduly.
- If your fund's performance seems out of line with its objective and it is lagging its benchmark and other similar funds, check that the reasons that you originally invested are still valid: Has the fund manager changed? Is the fund applying the same investment philosophy that produced its long-term record?

Independent advice

If you are uncertain about what to do, it is worthwhile consulting an independent financial adviser (IFA). An IFA can advise you on the most appropriate action. S/he will encourage you to remain invested during periods of underperformance if this will give you the potential to earn better long-term returns. Good advisers spend time and effort to weed out funds and managers that are not good long-term bets, and help you make switches that save you future losses. (Please see Jeanette Marais' piece on page 12, which discusses the merits of good, independent advice).

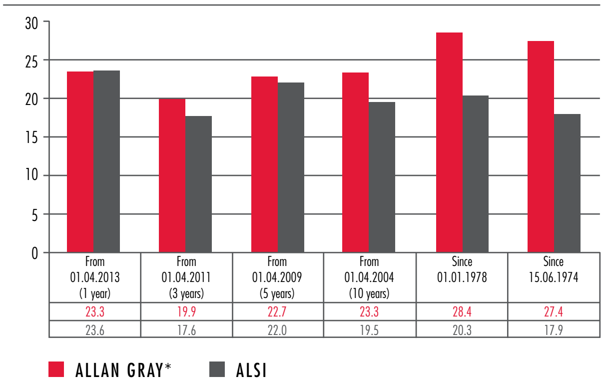
Thandi joined Allan Gray in 2008. She is a senior member of the distribution team, having previously worked in legal & compliance and marketing in the financial services sector. She completed her Masters of Business Law at the University of KwaZulu-Natal, has an advanced CFP from the University of the Free State and is an admitted attorney.

INVESTMENT TRACK RECORD – SHARE RETURNS

ALLAN GRAY PROPRIETARY LIMITED GLOBAL MANDATE SHARE RETURNS VS FTSE/JSE ALL SHARE INDEX

PERIOD	ALLAN GRAY*	FTSE/JSE ALL SHARE INDEX	OUT/UNDER-PERFORMANCE
1974 (from 15.06)	-0.8	-0.8	0.0
1975	23.7	-18.9	42.6
1976	2.7	-10.9	13.6
1977	38.2	20.6	17.6
1978	36.9	37.2	-0.3
1979	86.9	94.4	-7.5
1980	53.7	40.9	12.8
1981	23.2	0.8	22.4
1982	34.0	38.4	-4.4
1983	41.0	14.4	26.6
1984	10.9	9.4	1.5
1985	59.2	42.0	17.2
1986	59.5	55.9	3.6
1987	9.1	-4.3	13.4
1988	36.2	14.8	21.4
1989	58.1	55.7	2.4
1990	4.5	-5.1	9.6
1991	30.0	31.1	-1.1
1992	-13.0	-2.0	-11.0
1993	57.5	54.7	2.8
1994	40.8	22.7	18.1
1995	16.2	8.8	7.4
1996	18.1	9.4	8.7
1997	-17.4	-4.5	-12.9
1998	1.5	-10.0	11.5
1999	122.4	61.4	61.0
2000	13.2	0.0	13.2
2001	38.1	29.3	8.8
2002	25.6	-8.1	33.7
2003	29.4	16.1	13.3
2004	31.8	25.4	6.4
2005	56.5	47.3	9.2
2006	49.7	41.2	8.5
2007	17.6	19.2	-1.6
2008	-13.7	-23.2	9.5
2009	27.0	32.1	-5.1
2010	20.3	19.0	1.3
2011	9.9	2.6	7.3
2012	20.6	26.7	-6.1
2013	24.3	21.4	2.9
2014 (to 31.3)	7.0	4.3	2.7

RETURNS ANNUALISED TO 31.3.2014



* Allan Gray commenced managing pension funds on 1 January 1978. The returns prior to 1 January 1978 are of individuals managed by Allan Gray, and these returns exclude income. Returns are before fees.

Note: Listed property included from 1 July 2002. Inward listed included from November 2008 to November 2011.

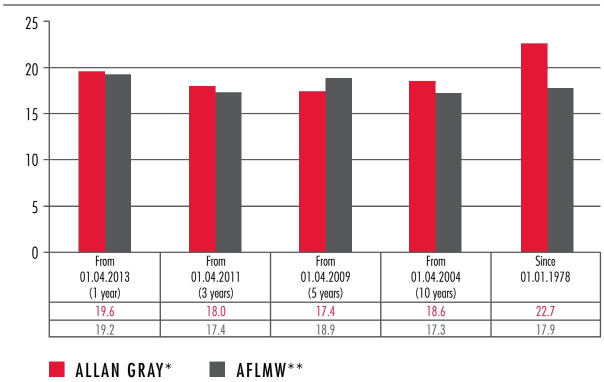
An investment of R10 000 made with Allan Gray on 15 June 1974 would have grown (before fees) to R152 051 485 by 31 March 2014. By comparison, the returns generated by the FTSE/JSE All Share Index (before any fees) over the same period would have grown a similar investment to R6 991 545.

INVESTMENT TRACK RECORD – BALANCED RETURNS

ALLAN GRAY PROPRIETARY LIMITED GLOBAL MANDATE TOTAL RETURNS VS ALEXANDER FORBES GLOBAL MANAGER WATCH

PERIOD	ALLAN GRAY*	AFLMW**	OUT/UNDER-PERFORMANCE
1974	-	-	-
1975	-	-	-
1976	-	-	-
1977	-	-	-
1978	34.5	28.0	6.5
1979	40.4	35.7	4.7
1980	36.2	15.4	20.8
1981	15.7	9.5	6.2
1982	25.3	26.2	-0.9
1983	24.1	10.6	13.5
1984	9.9	6.3	3.6
1985	38.2	28.4	9.8
1986	40.3	39.9	0.4
1987	11.9	6.6	5.3
1988	22.7	19.4	3.3
1989	39.2	38.2	1.0
1990	11.6	8.0	3.6
1991	22.8	28.3	-5.5
1992	1.2	7.6	-6.4
1993	41.9	34.3	7.6
1994	27.5	18.8	8.7
1995	18.2	16.9	1.3
1996	13.5	10.3	3.2
1997	-1.8	9.5	-11.3
1998	6.9	-1.0	7.9
1999	80.0	46.8	33.1
2000	21.7	7.6	14.1
2001	44.0	23.5	20.5
2002	13.4	-3.6	17.1
2003	21.5	17.8	3.7
2004	21.8	28.1	-6.3
2005	40.0	31.9	8.1
2006	35.6	31.7	3.9
2007	14.5	15.1	-0.6
2008	-1.1	-12.3	11.2
2009	15.6	20.3	-4.7
2010	11.7	14.5	-2.8
2011	12.6	8.8	3.8
2012	15.1	20.0	-4.9
2013	25.0	23.3	1.7
2014 (to 31.3)	3.9	2.6	1.3

RETURNS ANNUALISED TO 31.3.2014



** Consulting Actuaries Survey returns used up to December 1997. The return from 1 April 2010 is the average of the non-investable Alexander Forbes Large Manager Watch. The return for March 2014 is an estimate.

An investment of R10 000 made with Allan Gray on 1 January 1978 would have grown (before fees) to R16 496 553 by 31 March 2014. The average total performance (before fees) of global mandates of Large Managers over the same period would have grown a similar investment to R3 867 104.

ALLAN GRAY BALANCED AND STABLE FUND ASSET ALLOCATION AS AT 31 MARCH 2014

	BALANCED FUND % OF PORTFOLIO			STABLE FUND % OF PORTFOLIO		
	TOTAL	SA	FOREIGN*	TOTAL	SA	FOREIGN*
Net equities	55.5	43.7	11.8	17.2	13.3	4.0
Hedged equities	12.5	2.5	10.0	31.9	15.1	16.8
Property	1.6	1.2	0.4	2.2	1.9	0.3
Commodities	3.6	3.6	0.0	4.6	4.6	0.0
Bonds	10.0	9.6	0.3	8.5	8.3	0.1
Money market and bank deposits	16.9	13.6	3.3	35.7	32.1	3.6
TOTAL	**100.0**	**74.3**	**25.8**	**100.0**	**75.2**	**24.8**

Note: There might be slight discrepancies in the totals due to rounding.

* This includes African ex-SA assets.

ALLAN GRAY EQUITY FUND NET ASSETS AS AT 31 MARCH 2014

SECURITY (RANKED BY SECTOR)	MARKET VALUE (R MILLION)	% OF FUND	FTSE/JSE ALSI WEIGHT (%)
EQUITIES	**38 037**	**97.9**	
RESOURCES	**9 296**	**23.9**	**26.8**
Sasol	4 793	12.3	
Anglo American*	1 687	4.3	
BHP Billiton	726	1.9	
Impala Platinum	462	1.2	
Sibanye Gold	400	1.0	
Positions less than 1%	1 226	3.2	
FINANCIALS	**11 059**	**28.5**	**19.5**
Standard Bank	3 073	7.9	
Reinet Investments SA	1 623	4.2	
Old Mutual	1 333	3.4	
Investec	1 218	3.1	
Sanlam	944	2.4	
Barclays Africa	499	1.3	
Rand Merchant Insurance	477	1.2	
Positions less than 1%	1 892	4.9	
INDUSTRIALS	**17 496**	**45.0**	**53.7**
British American Tobacco	4 329	11.1	
SABMiller	3 203	8.2	
Remgro	2 032	5.2	
Netcare	605	1.6	
Nampak	574	1.5	
Sappi	563	1.4	
Mondi	503	1.3	
Tongaat Hulett	475	1.2	
Aspen Pharmacare	455	1.2	
Positions less than 1%	4 757	12.2	
OTHER SECURITIES	**186**	**0.5**	
COMMODITIES	**71**	**0.2**	
MONEY MARKET AND CALL DEPOSITS	**761**	**2.0**	
TOTALS	**38 870**	**100.0**	

* Including positions in Anglo American stub certificates.

ALLAN GRAY UNIT TRUSTS ANNUALISED PERFORMANCE IN PERCENTAGE PER ANNUM TO 31 MARCH 2014

UNIT TRUSTS[1]	QTR[3] (UNANNUALISED)	1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	ASSETS UNDER MANAGEMENT (R MILLION)	INCEPTION DATE
HIGH NET EQUITY EXPOSURE (100%)								
Allan Gray Equity Fund (AGEF)	-	**20.9**	**17.7**	**20.0**	**20.0**	**26.9**	38 869.6	01.10.98
FTSE/JSE All Share Index		23.6	17.6	22.0	19.5	19.0		
Allan Gray-Orbis Global Equity Feeder Fund (AGOE)	-	**44.9**	**29.8**	**22.6**	**-**	**16.2**	13 213.5	01.04.05
FTSE World Index (Rands)		35.5	27.2	21.2	-	13.8		
MEDIUM NET EQUITY EXPOSURE (40% - 75%)								
Allan Gray Balanced Fund (AGBF)	-	**18.8**	**16.6**	**16.1**	**17.0**	**19.6**	89 425.5	01.10.99
Average of South African - Multi Asset - High Equity category (excl. AGBF)[10]		16.7	14.9	15.7	15.3	14.3		
Allan Gray-Orbis Global Fund of Funds (AGGF)	-	**32.5**	**24.7**	**14.2**	**12.3**	**11.4**	11 433.9	03.02.04
60% of the FTSE World Index and 40% of the JP Morgan Global Government Bond Index (Rands)		27.4	23.8	15.3	12.4	11.1		
LOW NET EQUITY EXPOSURE (20% - 40%)								
Allan Gray Stable Fund (AGSF)	-	**11.0**	**11.5**	**9.7**	**12.0**	**13.5**	35 009.9	01.07.00
Daily interest rate of FirstRand Bank Limited plus 2%		6.2	6.4	7.1	8.4	9.4		
VERY LOW NET EQUITY EXPOSURE (0% - 20%)								
Allan Gray Optimal Fund (AGOF)	-	**4.8**	**4.6**	**4.6**	**6.8**	**7.8**	837.8	01.10.02
Daily interest rate of FirstRand Bank Limited		4.2	4.3	5.0	6.3	6.8		
Allan Gray-Orbis Global Optimal Fund of Funds (AGOO)	-	**24.0**	**19.2**	**-**	**-**	**11.4**	1 543.6	02.03.10
Average of US$ Bank Deposits and Euro Bank deposits		19.1	15.9	-	-	8.9		
NO EQUITY EXPOSURE								
Allan Gray Bond Fund (AGBD)	-	**3.0**	**9.0**	**9.2**	**-**	**9.2**	627.1	01.10.04
BEASSA All Bond Index (total return)		0.6	9.2	9.0	-	8.9		
Allan Gray Money Market Fund (AGMF)	-	**5.3**	**5.4**	**6.2**	**7.6**	**8.3**	7 988.5	03.07.01
Alexander Forbes Short Term Fixed Interest (STeFI) Composite Index[9]		5.3	5.4	6.1	7.5	8.2		

ALLAN GRAY TOTAL EXPENSE RATIOS (TERS)

	EQUITY FUND	GLOBAL EQUITY FEEDER FUND	BALANCED FUND	GLOBAL FUND OF FUNDS	STABLE FUND	OPTIMAL FUND	GLOBAL OPTIMAL FUND OF FUNDS	BOND FUND	MONEY MARKET FUND
Performance fees	0.44%	0.49%	0.44%	1.25%	0.80%	0.00%	1.81%	0.23%	N/A
Fee for benchmark performance	1.50%	1.49%	1.06%	1.22%	1.02%	1.00%	0.99%	0.25%	0.25%
Other costs including trading costs	0.06%	0.18%	0.09%	0.23%	0.09%	0.08%	0.25%	0.02%	0.01%
VAT	0.27%	0.00%	0.12%	0.00%	0.16%	0.15%	0.00%	0.07%	0.04%
TOTAL EXPENSE RATIO (TER)	2.27%	2.16%	1.71%	2.70%	2.07%	1.23%	3.05%	0.57%	0.30%

A Total Expense Ratio (TER) of a portfolio is a measure of the portfolio's assets that were relinquished as a payment of services rendered in the management of the portfolio. The total operating expenses are expressed as a percentage of the average value of the portfolio, calculated for the year to 31 December 2013. Included in the TER is the proportion of costs incurred by the performance component, fee at benchmark and other expenses. These are disclosed separately as percentages of the net asset value. Trading costs (including brokerage, VAT, STT, STRATE, levy and insider trading levy) are included in the TER.
A high TER will not necessarily imply a poor return nor does a low TER imply a good return. The current TER cannot be regarded as an indication of future TERs.

ORBIS FUNDS ANNUALISED PERFORMANCE IN PERCENTAGE PER ANNUM TO 31 MARCH 2014

	QTR (UNANNUALISED)	1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	INCEPTION DATE
ORBIS FUNDS (RANDS) REGISTERED FOR MARKETING IN SOUTH AFRICA[1, 6]							
Orbis Global Equity Fund (Rands)	**-0.9**	**44.6**	**29.9**	**22.5**	**15.3**	**19.5**	01.01.90
FTSE World Index (Rands)	1.5	35.1	27.1	21.1	13.4	13.4	
Orbis SICAV Japan Equity (Yen) Fund (Rands)	**-3.2**	**27.2**	**28.3**	**17.3**	**10.1**	**15.2**	01.01.98
Tokyo Stock Price Index (Rands)	-4.8	23.9	22.8	12.7	7.5	8.1	
Orbis SICAV Asia Ex-Japan Equity Fund (Rands)	**-1.6**	**31.0**	**23.8**	**23.6**	**-**	**18.0**	01.01.06
MSCI Asia Ex-Japan (Rands)	-0.6	17.5	16.8	18.5	-	14.9	
Orbis Optimal SA Fund-US$ Class (Rands)	**-1.0**	**22.0**	**19.7**	**6.4**	**-**	**11.6**	01.01.05
US$ Bank Deposits (Rands)	0.1	14.5	16.1	2.2	-	9.1	
Orbis Optimal SA Fund-Euro Class (Rands)	**-0.9**	**29.6**	**18.6**	**6.7**	**-**	**11.2**	01.01.05
Euro Bank Deposits (Rands)	0.3	22.9	15.4	3.3	-	9.0	

SEGREGATED AND LIFE POOLED PORTFOLIOS ANNUALISED PERFORMANCE IN PERCENTAGE PER ANNUM TO 31 MARCH 2014

	QTR[3] (UNANNUALISED)	1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	ASSETS UNDER MANAGEMENT (R MILLION)	INCEPTION DATE
SEGREGATED PORTFOLIOS[5] (BEFORE FEES, EXCEPT FOR FUNDS INDICATED BY FOOTNOTE 1)								
Domestic Equity Composite FTSE/JSE All Share Index	**7.0** 4.3	**22.2** 23.6	**18.7** 17.6	**21.5** 22.0	**23.0** 19.5	**22.0** 15.4	63 386.6	01.01.90
Domestic Balanced Composite Mean of Alexander Forbes Domestic Manager Watch[2,7]	**5.2** 3.5	**14.6** 16.0	**14.7** 15.0	**16.9** 18.8	**19.4** 18.0	**23.0** 18.2	22 750.4	01.01.78
Global Balanced Composite Mean of Alexander Forbes Global Large Manager Watch[2,4]	**3.9** 2.6	**19.6** 19.2	**18.0** 17.4	**17.4** 18.9	**18.6** 17.3	**22.7** 17.9	61 234.7	01.01.78
Global Balanced Namibian High Foreign Composite Mean of Alexander Forbes Namibia Average Manager[2]	**3.0** 2.7	**19.7** 19.2	**18.3** 16.7	**16.2** 18.2	**18.1** 17.1	**19.7** 14.9	8 773.0	01.01.94
Foreign Best View (Rands) Composite[1,8] 60% of the MSCI World Index[11] and 40% of the JP Morgan Global Government Bond Index (Rands)	**-0.2** 2.0	**31.9** 26.3	**24.8** 23.4	**13.8** 15.1	**12.3** 12.3	**15.2** 12.0	5 672.2	23.05.96
Relative Domestic Equity Composite Weighted average of client specific benchmarks[2]	**5.3** 4.7	**25.2** 24.4	**18.6** 18.3	**22.0** 22.4	**21.2** 19.9	**21.6** 17.2	2 865.5	19.04.00
LIFE POOLED PORTFOLIOS (BEFORE FEES, EXCEPT FOR FUNDS INDICATED BY FOOTNOTE 1)								
Domestic Equity Portfolio FTSE/JSE All Share Index	**7.0** 4.3	**23.3** 23.6	**19.4** 17.6	**22.1** 22.0	**23.3** 19.5	**24.2** 16.9	7 658.4	01.02.01
Domestic Balanced Portfolio Mean of Alexander Forbes Domestic Manager Watch[2,7]	**5.1** 3.5	**14.5** 16.0	**15.2** 15.0	**17.3** 18.8	**19.7** 18.0	**20.2** 17.1	4 982.3	01.09.01
Global Balanced Portfolio Mean of Alexander Forbes Global Large Manager Watch[2,7]	**3.9** 2.6	**19.7** 19.2	**18.3** 17.4	**17.7** 18.9	**18.7** 17.3	**20.3** 15.7	30 966.2	01.09.00
Domestic Stable Portfolio Alexander Forbes Three-Month Deposit Index plus 2%	**3.8** 1.8	**8.8** 7.2	**8.7** 7.4	**10.0** 8.0	**13.6** 9.5	**14.4** 10.3	2 125.3	01.12.01
Global Stable Portfolio Alexander Forbes Three-Month Deposit Index plus 2%	**2.9** 1.8	**12.8** 7.2	**12.8** 7.4	**10.9** 8.0	**-** -	**13.9** 9.5	4 745.5	15.07.04
Domestic Absolute Portfolio Mean of Alexander Forbes Domestic Manager Watch[7]	**5.6** 3.5	**7.5** 16.0	**8.7** 15.0	**12.0** 18.8	**17.5** 18.0	**20.7** 16.8	564.0	06.07.01
Global Absolute Portfolio Mean of Alexander Forbes Global Large Manager Watch[2,7]	**3.9** 2.6	**12.9** 19.2	**12.9** 17.4	**13.1** 18.9	**17.7** 17.3	**17.7** 17.2	3 655.3	01.03.04
Orbis Global Equity Portfolio[1] FTSE World Index (Rands)	**-0.9** 1.5	**44.7** 35.1	**29.8** 27.1	**22.5** 21.1	**-** -	**15.8** 13.4	5 566.8	18.05.04
Foreign Portfolio[1] 60% of the MSCI World Index[11] and 40% of the JP Morgan Global Government Bond Index (Rands)	**-0.3** 2.0	**31.6** 26.3	**24.6** 23.4	**13.7** 15.1	**12.3** 12.3	**8.5** 6.5	882.4	23.01.02
Hedged Domestic Equity Portfolio FTSE/JSE CAPI Index	**6.8** 4.3	**21.8** 23.5	**18.1** 17.9	**20.7** 22.4	**-** -	**13.9** 11.4	1 225.2	01.06.08
Relative Domestic Equity Portfolio FTSE/JSE CAPI Index	**5.1** 4.3	**24.6** 23.5	**17.7** 17.9	**21.2** 22.4	**21.0** 20.1	**23.4** 22.2	261.9	05.05.03
Domestic Optimal Portfolio[1] Daily Call Rate of Nedcor Bank Limited	**2.0** 1.1	**5.9** 4.4	**5.5** 4.6	**5.5** 5.2	**7.7** 6.6	**8.3** 7.0	393.0	04.12.02
Domestic Medical Scheme Portfolio Consumer Price Index plus 3% p.a.[2]	**3.7** 3.7	**8.4** 9.1	**8.7** 9.1	**9.9** 8.6	**-** -	**12.9** 9.2	1 465.2	01.05.04
Money Market Portfolio[1] Alexander Forbes Three-Month Deposit Index	**1.4** 1.3	**5.4** 5.1	**5.6** 5.3	**6.4** 5.9	**7.7** 7.4	**8.7** 8.3	170.0	21.09.00

PERFORMANCE AS CALCULATED BY ALLAN GRAY

1 The fund returns are net of investment management fees
2 The return for the period ending 31 March 2014 is an estimate as the relevant survey results have not yet been released
3 Unable to disclose due to ASISA regulations
4 Consulting Actuaries Survey returns used to 31 December 1997. Alexander Forbes Global Large Manager Watch used from 1 January 1998. Alexander Forbes Non-Investable Global Large Manager Watch used from 1 April 2010
5 The composite assets under management figures shown include the assets invested in the pooled portfolios above where appropriate
6 Amounts invested by the Allan Gray client portfolios in the Orbis funds are included in the assets under management figures in the table above
7 The mean returns of the Alexander Forbes Non-Investable Large Manager Watch used from 1 April 2010
8 The foreign carve-out returns of the Global Balanced Composite used from 23 May 1996 to 31 August 2001. The Foreign Balanced Composite returns are used from 1 September 2001
9 Alexander Forbes Three-Month Deposit Index from 3 July 2001 to 31 March 2003. As from 1 April 2003, the benchmark is the simple average of the Domestic Fixed Interest Money Market Unit Trust Sector excluding the Allan Gray Money Market Fund. The benchmark from 1 November 2011 is the Alexander Forbes Short Term Fixed Interest (STeFI) Composite Index
10 The benchmark was the daily weighted average of the Domestic Prudential Medium Equity Unit Trust sector excluding Allan Gray Balanced Fund from inception until 31 December 2007. With effect from 1 January 2008 it was changed to the daily weighted average (based on assets under management) of the Domestic Prudential Medium Equity Unit Trust Sector and the Prudential Variable Equity Sector excluding Allan Gray Balanced Fund. The change was as a result of the Allan Gray Balanced Fund being reclassified from the Domestic Prudential Medium Equity Sector to the new Prudential Variable Equity Sector. The benchmark from 1 February 2013 is the daily weighted average return of funds in the South African - Multi Asset - High Equity category (excluding the Allan Gray Balanced Fund)
11 Morgan Stanley Capital International All Country World Index

THE ALLAN GRAY GROUP	
UNIT TRUSTS	A unit trust is a savings vehicle for investors who want to grow their money and may want to access it before they retire. Unit trusts allow investors to pool their money with other investors who have similar investment objectives. Unit trusts are also known as 'portfolios of collective investment schemes' or 'funds'. Allan Gray has nine funds in its stable: Equity, Balanced, Stable, Optimal, Money Market, Bond, Global Equity Feeder, Global Fund of Funds and Global Optimal Fund of Funds.
RETIREMENT ANNUITY*	The Allan Gray Retirement Annuity Fund (RA) is a savings vehicle for investors looking for a flexible, tax-efficient way to save for retirement. Investors can only access their money when they retire. Individually owned RAs can be managed on a group basis, offering employers a flexible solution to the challenge of retirement funding for their staff.
PRESERVATION FUNDS*	The Allan Gray Pension Preservation and Provident Preservation funds are savings vehicles for investors looking for a tax-efficient way to preserve existing retirement benefits when they leave a pension or provident fund, either as a result of a change in employment (e.g. retrenchment or resignation), or when they transfer from another preservation fund.
ENDOWMENT*	The Allan Gray Endowment Policy is a savings policy for investors who want a tax-efficient way to save and wish to create liquidity in their estate.
LIVING ANNUITY*	The Allan Gray Living Annuity gives investors flexibility, within certain regulatory limits, to select an annuity best suited to their income needs after retirement. A living annuity provides investors with a regular income which is not guaranteed, and which is funded by growth on capital and income from interest and dividends.
OFFSHORE FUNDS	Through our partnership with Orbis we offer you a cost-effective way to diversify your portfolio by investing offshore. There are two options for investing offshore through Allan Gray: invest in rand-denominated offshore funds without the need to use your offshore investment allowance, or use your offshore investment allowance to invest in foreign funds.
PLATFORM – LOCAL AND OFFSHORE	Our investment platform provides you with access to all of our products, as well as a focused range of unit trusts from other fund providers. The platform enables you to buy, sell and switch – usually at no charge – between the funds as your needs and objectives change. South African investors who wish to diversify their portfolios can also access funds from certain other offshore fund providers via the same platform.
LIFE POOLED PORTFOLIOS	The minimum investment per client is R20 million. Mandates include risk-profiled pooled portfolios: Stable Portfolio, Balanced Portfolio and Absolute Portfolio; asset class pooled portfolios: Money Market, Equity and Foreign, and finally an Optimal Portfolio.
SEGREGATED PORTFOLIOS	The minimum portfolio size is R500 million. Mandates are of a balanced or asset class specific nature. Portfolios can be managed on an absolute or relative risk basis.
BOTSWANA	Allan Gray Botswana manages institutional portfolios on a segregated basis and offers our range of nine South African unit trusts to individual investors.
NAMIBIA	Allan Gray Namibia manages institutional portfolios on a segregated basis and the Allan Gray Namibia Investment Trust provides investment management for Namibian retirement funds in a pooled vehicle.
SWAZILAND	Allan Gray Swaziland manages institutional portfolios on a segregated basis.
ALLAN GRAY ORBIS FOUNDATION	Allan Gray Orbis Foundation is a non-profit organisation that was established in 2005 as an education and development catalyst. It seeks to foster a next generation of high-impact leaders and entrepreneurs for the ultimate purpose of increased job creation in Southern Africa. The Foundation focuses on educational and experiential methods at the secondary and tertiary levels to realise the potential of bright young minds. Through its highly-researched learning programmes, it intends to equip talented young individuals with the skills, attitudes and motivation to have a significant future impact.
E^2	E^2 stands for 'excellence in entrepreneurship' and as a long-term capital fund its purpose is to provide substantial financing to entrepreneurs who are graduates of the Allan Gray Fellowship Programme. In addition, E^2 provides financing for social entrepreneurs who demonstrate exceptional leadership and creative initiative in the not-for-profit sectors.

* This product has unit trusts as its underlying investment option.

Directors

Executive

M Cooper	BBusSc FIA FASSA
R W Dower	BSc (Eng) MBA
I S Liddle	BBusSc (Hons) CFA
T Mhlambiso	AB MBA JD

Non-Executive

W B Gray	BCom MBA CFA (Irish)
T J Mahuma	BA (Hons) MPhil
S C Marais	PhD CFA
K C Morolo	BSc (Eng) MEng

Company Secretary

CE Solomon BBusSc (Hons) CA (SA)

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