



Q2

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QUARTERLY
COMMENTARY

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me?

AngloGold
Ashanti:
Poised to benefit

Sappi - Frogs
can make good
investments,
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History rhyming?
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Greg Fury

COMMENTS FROM THE CHIEF OPERATING OFFICER

Readers of the Quarterly Commentary will have noticed that similar themes recur over several issues. In recent times, we have expressed concern about the level of overall asset prices, in particular the dollar value of South African shares listed on the JSE. This is not because overall PE ratings on current earnings look too high, but more because we believe that company earnings are at very high levels and are at risk of falling. This means that the true PE ratio on 'normal' future earnings is much higher. We have also expressed an increasing level of concern about the inflation outlook.

These issues come together in the article by portfolio manager Duncan Artus who argues that higher global inflation could be the underlying cause of a decline in company earnings. All things being equal, lower earnings will mean declines in share prices.

So what are we doing about this concern? While there has been some change in asset allocation (the conventional retreat to cash), our balanced portfolios retain a substantial portion of South African shares, but this is concentrated in companies that we believe will be able to grow their earnings in future – readers can see the holdings of a typical client portfolio, the Allan Gray Balanced Fund, towards the back of the Quarterly Commentary. These are mainly high quality, globally diversified businesses that may not look obviously 'cheap', but which have proven their ability to maintain and grow earnings even in tough times. In the recent past we have discussed examples like Richemont and SABMiller. Our portfolios also include some 'cyclical' companies whose earnings we believe are below normal levels. In this issue we focus on Sappi and AngloGold Ashanti.

Based on its inconsistent profitability track record, Sappi would not exemplify a typical 'high quality' company. However, investors who believe only historically 'good' companies make sound investments could miss opportunities to earn substantial returns. The best opportunities are often presented by cyclical companies when their earnings are depressed and most investors expect them to remain low. Delphine Govender explains why Allan Gray believes the stage is set for Sappi's earnings to return to more normal levels.

Like many South African mining companies, AngloGold Ashanti has not enjoyed the benefit of much higher commodity (in this case gold) prices as dramatic cost increases have eroded revenue gains. In addition, the company sold a large part of its future production forward at much lower gold prices than those that currently prevail. Nevertheless, a new management team, together with substantial investments and promising exploration assets, leave it well positioned to benefit from the current high gold price.

Over time, every company and each sector of the stockmarket move back and forth between seasons of outperformance and seasons of underperformance, and often these cycles differ for different sectors of the market. Matthys de Kock notes that the tendency for Allan Gray's share portfolio has been to underperform the market in times when the prices of the major sectors move to extremes relative to one another – when already irrational pricing becomes even more irrational. This, we believe, could be the case at present. The good news, however, is that over the long term the market is a very good judge of value and wide disparities tend to be temporary and reverse, giving contrarian investors great opportunities.

On a very positive note, I am pleased to announce that Simon Raubenheimer has been promoted to the position of portfolio manager from 1 July. Simon is a product of our established process, having spent his entire investment career at Allan Gray, and having progressed from trainee analyst to portfolio manager. He has been with the firm since February 2002 and holds a B Com (Econometrics) from the University of Pretoria and a B Com Honours (Finance) degree from UCT and is a CFA Charterholder. Readers of the Quarterly Commentary will recall his recent articles on British American Tobacco and Richemont. We have great confidence in Simon and high expectations.

Kind regards

Greg Fury



Duncan Artus

WHAT'S WORRYING ME?

EXECUTIVE SUMMARY: Company earnings are at very high levels, underpinning the high returns of the past few years. But what will cause earnings to fall? Duncan Artus explores some possibilities and concludes that the trend that is very likely to spoil the earnings party could well be the re-emergence of significant global inflation. Allan Gray has positioned its clients' portfolios over the past few years with this view on earnings in mind.

People outside the investment management industry often ask me what exactly it is that we do. After much thought, my standard reply has become 'we are paid to worry'. At Allan Gray we manage a not-insignificant portion of the South African savings pool. This is a responsibility we take very seriously and our top priority is attempting to maintain our clients' wealth in real terms when the risk of loss is high.

For some time now, we have been communicating to investors in our funds that the absolute returns they have enjoyed in the recent past have been unsustainably high and that the potential grenade in the tea party could well be a sharp correction in company earnings which are at very high levels.

Graph 1 and **Graph 2** depict the level of real earnings for local and developed market equities. Even a cursory glance reveals that real earnings are at very high levels globally.

Having highlighted the high level of earnings as depicted in Graph 1 and 2 on numerous occasions, the natural thought that springs to mind is, 'well, that's a nice chart but what will cause earnings to fall?'. We spend a lot of time thinking about the level of earnings in all the businesses we are currently analysing when considering their inclusion in the portfolio.

Unfortunately, the prospect or cause of a future fall in company profits is seldom glaringly apparent before the fall, although it can often appear 'obvious' with the benefit of hindsight. The longer and stronger the trend has been, the less likely investors are to see and appreciate the consequences of the turning point at the time. We found the following quote by Jim Grant to be particularly relevant to current markets:

"Financial epochs come and go on little cat feet. Nobody issues a press release to herald their arrival. And no one rings a bell

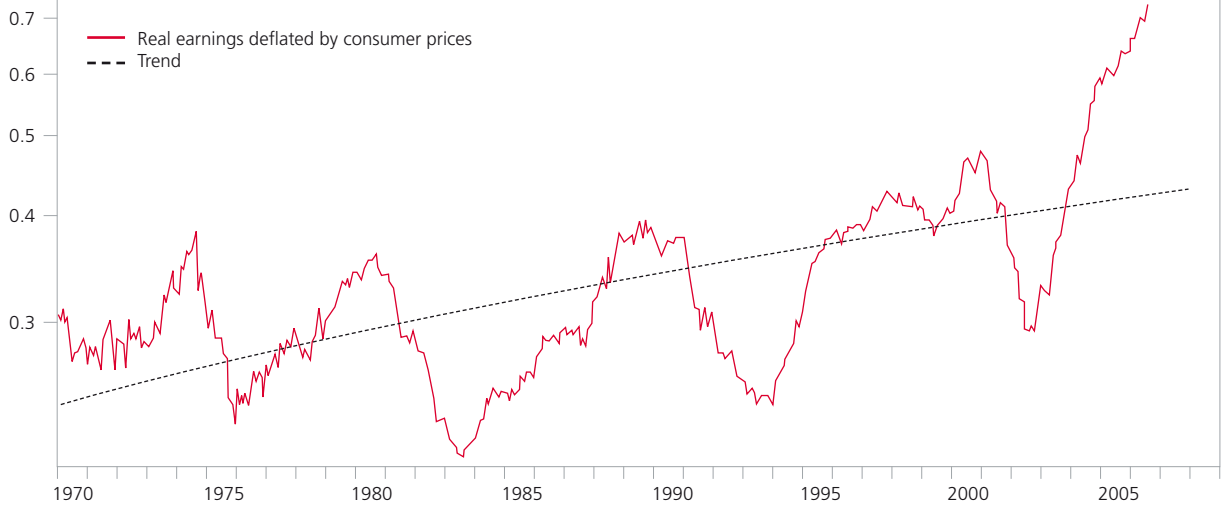
to toll their departure. One day, people wake up to discover that the world has changed. 'How did that happen?' they wonder." Jim Grant, Grant's Interest Rate Observer

So we thought we would wonder in advance and consider a few issues that could cause an energetic ringing of the bell. We do this accepting that we are very unlikely to be smart or lucky enough to predict the exact nature or timing thereof. Indeed, it may be some time before the bell breaks its silence. Investment management can sometimes be a frustrating business!

Real earnings are cyclical around their long-term trend (see Graphs 1 and 2). Typically, when profits have been high for some time, we would expect to see a rise of more populist governments, higher taxes, increased demands by labour and simple supply/demand dynamics (new producers entering an industry chasing high profits) applying inevitable downward pressure on profits. Meanwhile, a sharper correction may be brought about by an unforeseen event and the consequences thereof.

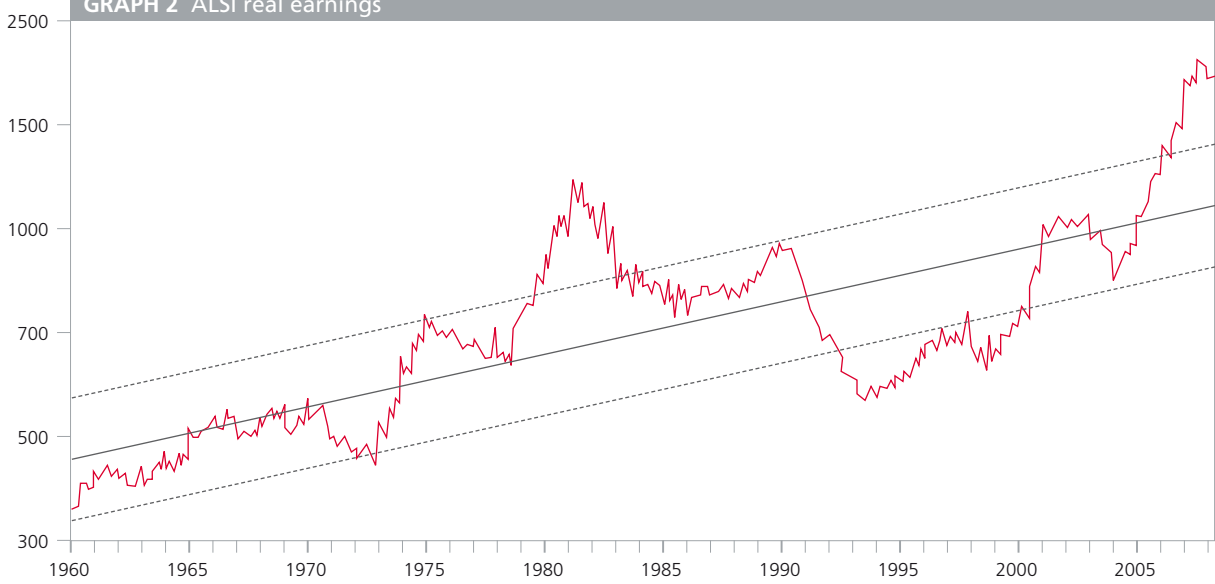
The trend or event that spoils the earnings party could well be the re-emergence of significant global inflation (see Sandy McGregor's article in Quarterly Commentary Q1, 2008), especially considering the fact that inflation is roaring ahead in the low-wage countries of Asia. They have been highly efficient exporters of deflation to the global economy, allowing it to absorb high commodity prices and a weak dollar. **Graph 3** highlights the significant recent increase in Chinese inflation. This has affected many local companies who import product from China, while many global businesses that operate in China have seen a material increase in their operating costs.

GRAPH 1 Real global corporate profits in Organisation for Economic Co-operation and Development countries



Source: The Bank Credit Analyst (earnings are Morgan Stanley Capital International Data)

GRAPH 2 ALSI real earnings



Source: I-Net

We see a few important repercussions for company earnings

1. Input cost inflation will clearly squeeze the profitability of businesses unable to pass on a significant portion of this cost increase to an increasingly wary and price-sensitive global consumer.
2. In our view, interest rates will have to rise across the world (especially in the United States where a weak dollar will exacerbate the effect of Asian inflation). This will increase the cost of servicing debt and reduce the ability of businesses to leverage their balance sheets.
3. Higher interest rates normally translate into higher discount rates, which are used to value assets. It is not often appreciated that higher asset prices themselves can lead to higher earnings which in turn lead to higher asset prices. This virtuous circle also works in reverse as Jack Mitchell, former portfolio manager and director of

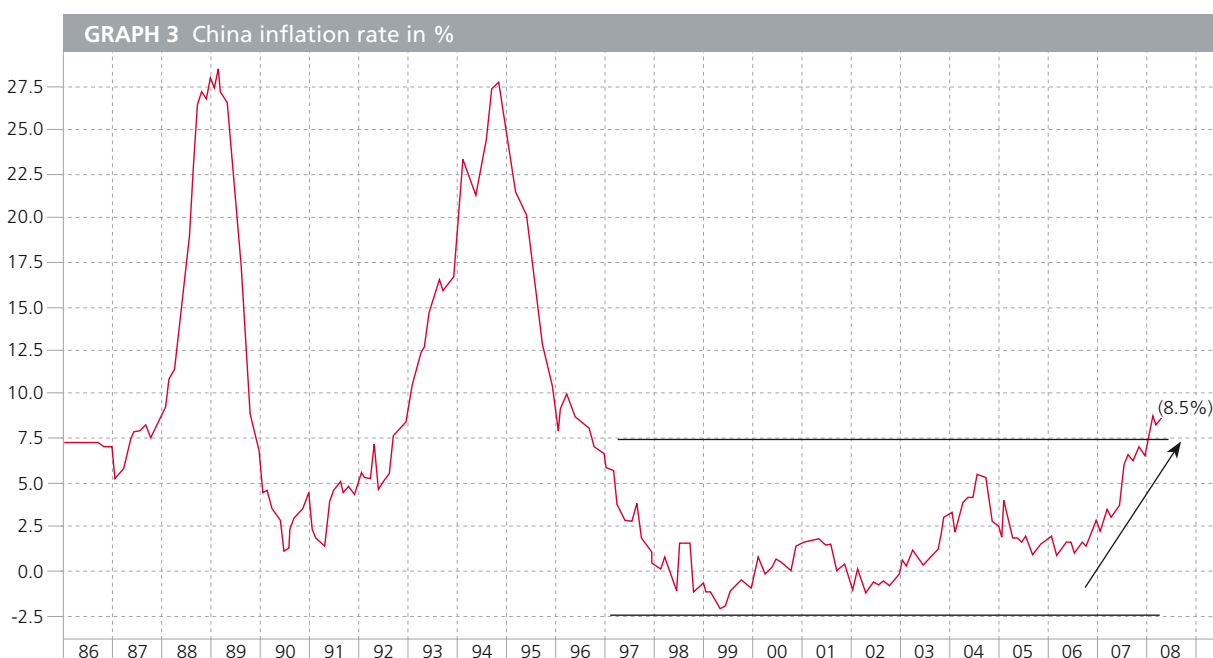
Allan Gray, used to remind us, 'nothing ends high prices like high prices'.

So how can we position our clients' portfolios, given these potential concerns?

The high levels of absolute returns provided by South African assets in the recent past have been aided by almost all the reasons earnings are high globally. The drivers of this boom such as commodities, emerging markets, property, hedge funds, easy credit and increased appetite for risk have all dovetailed favourably for local asset prices. New bull markets are very rarely led by the same sectors or factors that led the previous advance.

The correct investment strategy is not that obvious as highlighted by two simple examples

1. When investors are concerned about the level of future



Source: I-Net

equity returns, they often seek refuge in assets uncorrelated with equities as a means to lower risk. The problem is that historical correlations can change over time. For example, **Graph 4** highlights the increasingly positive correlation of hedge funds and the S&P 500. Not all hedge funds may turn out to be the low volatility investments they claim to be.

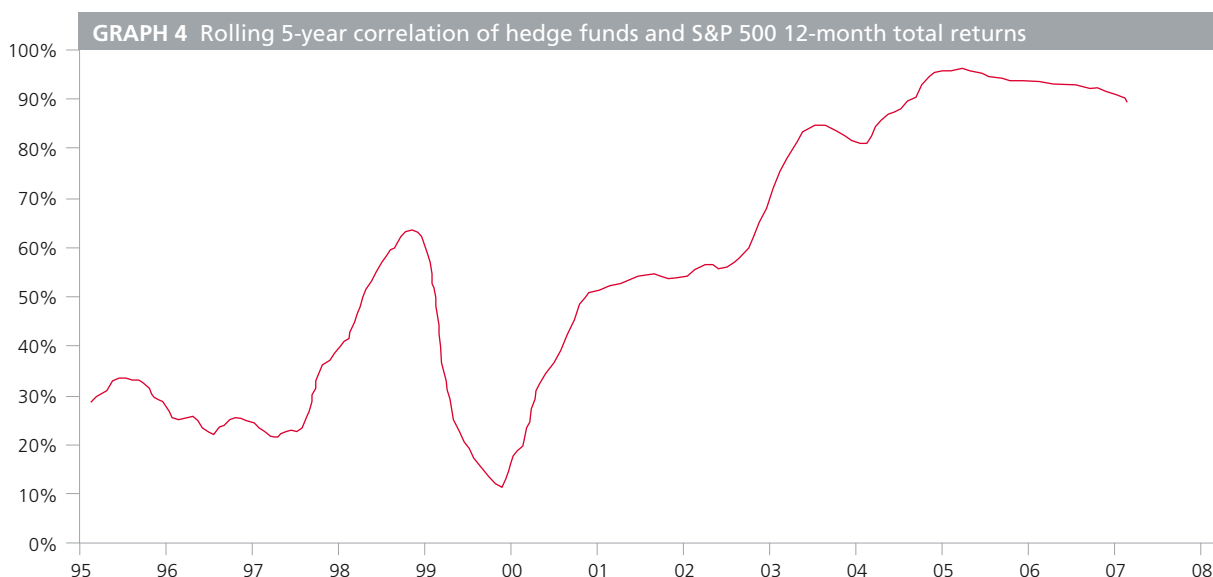
2. Fixed income (bonds and cash) may not either be the safe-haven many investors assume them to be. Fixed income investments should be increasingly vulnerable to a secular increase in inflation after a long decline in global yields. Investors may demand a return to real yields (interest rates greater than inflation) which they have been happy to forego as the capital appreciation has more than offset the negative real yield.

Given that we are very unlikely to call accurately the turning points or events that will drive returns down to more normal levels, we have carefully positioned the portfolios to try to maintain (hopefully even grow) our clients' wealth in real terms.

For some time now, a significant portion of our clients' portfolios has been invested in high quality, globally diversified businesses that have a reasonable probability of growing their earnings in real terms. Businesses that are able to generate this real growth in earnings are going to become increasingly scarce as growth dissipates and we believe that this ability will become increasingly valuable as earnings revert to long-term trend.

We continue to have a significant exposure to our chosen shares as we believe them to be better stores of wealth over our investment horizon than simply holding greater quantities of bonds and cash. In addition, as our clients are well aware, approximately 10% of fund is invested in gold and gold producers, our fixed income duration is very short and, where we have discretion, we have the maximum allowable weighting in offshore assets.

However, we continue to caution investors that these expected real returns are by no means likely to accrue in an orderly fashion. In fact we would be very surprised if they did.



Source: Merrill Lynch



Andrew Lapping

ANGLOGOLD ASHANTI: POISED TO BENEFIT

EXECUTIVE SUMMARY: AngloGold Ashanti, like most gold mining companies, has seen dramatic cost increases erode revenue gains. It also has to deal with a large hedge book. Nevertheless, a new management team, hedge restructuring and its promising exploration portfolio leave it well positioned to benefit from a high gold price. As Andrew Lapping explains, these factors make the company Allan Gray's preferred gold investment.

Over the past three years the rand gold price has appreciated by 159%, outpacing the FTSE/JSE All Share Index (ALSI) return of 146%. One would expect South African listed gold shares to have exhibited similarly impressive results. Unfortunately, this has not been the case (see **Graph 1**) as dramatic cost increases have eroded revenue gains and resulted in South African gold shares underperforming the ALSI by 33% over the same period.

There are many causes of cost inflation in the mining industry

An acute skills shortage, particularly of experienced personnel, has forced wage rates upwards. Commodity companies consume commodities (such as steel) themselves, further driving up input costs. Adding to these woes, South African gold mines are deep and, in some cases, approaching the end of their lives. These factors have a significant impact on costs as companies mine the easier, higher grade portions on a mine first, leaving higher cost, lower grade areas for the end of a mine's life.

The average unit cash cost of South African underground gold mines has increased by 72% over the past five years, significantly more than the consumer price index increase of 27.5%. This equates to a 6.5% real cost escalation per year. The reported cash cost of producing a unit of gold would have been even higher had the industry not changed the way it treats development costs. These costs are now excluded from cash costs.

Given poor cost controls, investors may conclude that gold shares will never benefit from a high gold price and

they may prefer to invest in physical gold as a way to ensure participation in the gold price. However, we are of the view that certain gold shares will participate in further gold price appreciation and profit from the current gold price. We believe AngloGold Ashanti, our largest gold share investment, is well poised to benefit from the current gold price. AngloGold has aspects that we like: new management; a portfolio of assets with unrealised potential; a class leading exploration portfolio and a declining hedge book.

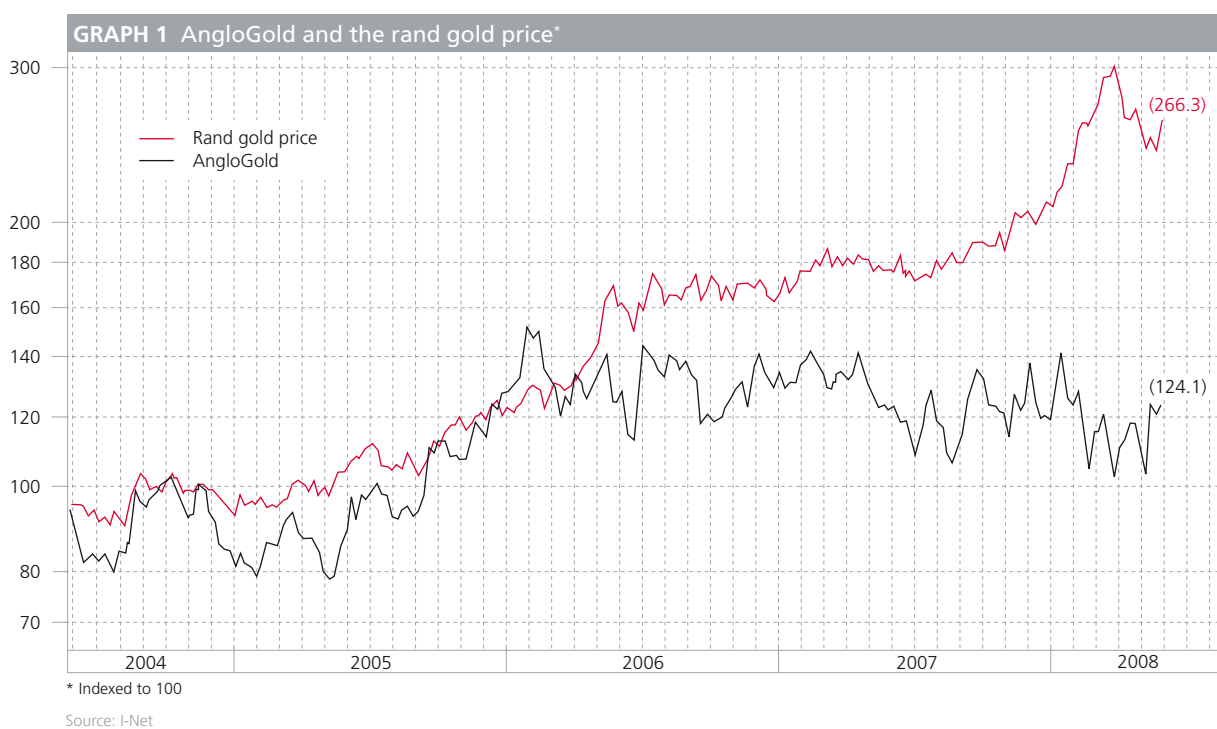
What makes AngloGold a preferred gold investment?

"We believe AngloGold Ashanti, our largest gold share investment, is well poised to benefit from the current gold price."

We feel that Mark Cutafani, the new CEO, together with a restructured executive management team, can make a significant difference to the company. The new team has adopted a value based approach: rather than simply continuing to operate assets in a steady manner, management is looking to extract maximum value from all the assets in the company. In an effort to extract this value,

all possibilities are being considered, from growing production to maximise net present value, to selling assets to a company that may pay a premium for strategic reasons. It is our experience that a new, revitalised management focused on unlocking shareholder value can make a surprisingly large impact. AngloGold management now needs to turn ideas into results. We believe it has the requisite skills to do so.

The past year has been a difficult one for some of AngloGold's key profit generators, most notably Geita, a large Tanzanian open pit mine. A few of the South African and South



American mines also had production issues during the period. AngloGold, just like all other mining companies, is struggling to control costs in the face of extensive input cost inflation. A mitigating factor is that some of AngloGold's assets are coming off a low base. The cost profile of the portfolio should improve as Geita returns to a steady state of production and new projects start production, offsetting some of the cost pressures. This should allow AngloGold's cost escalations to better the industry average and allow the higher gold price to flow through to the bottom line. Various capital projects approaching completion should lower AngloGold's cash cost and as the new projects come on line, capital expenditure should moderate, boosting cash flows. A further attraction to AngloGold is the globally diversified nature of its operations and the fact that any region-specific cost issues are not company-threatening.

Over the years, AngloGold has made large investments in exploration. These investments are now beginning to deliver results. The most exciting developments are in Colombia where AngloGold recently announced the discovery of a 12.9 million ounce resource. AngloGold had the 'first mover' advantage in Colombia and did preliminary work on most of the Colombian Andes. The company has narrowed its permit area down to 37 500 square kilometres, an area twice the size of the Kruger National Park. In addition to the gold opportunities being investigated, the company is studying 104 base metal anomalies with its partner Glencore.

Together with the Colombian exploration, AngloGold has made exciting discoveries in Australia and the Democratic Republic of the Congo. The Tropicana discovery in Australia will almost certainly become a mine.

Deterrents for potential AngloGold investors

The large hedge book is the number one deterrent. The reason is that gold share investors, by their very nature, are bullish on gold and looking for leverage to the gold price. The hedge steals this leverage and is very dangerous in an environment of rapid cost inflation.

When hedging, a company sells forward a specific quantity of gold at a predetermined price for delivery on a specific future date. Hedging is usually done to 'lock in' profits. When the transaction is entered into, the hedge may look sensible as the production costs, at the time, are known and the future selling price is known. If the costs increase as expected, a hedge locks in the margin and reduces the business risk.

However, predicting the future is exceedingly difficult and the eventual outcome, whether on costs or actual production, is often one that was never thought possible.

The most effective way for a commodity company to reduce business risk is to focus on the operations and ensure the company is correctly positioned on the cost curve. In the case of AngloGold, and the entire gold industry, an unexpected outcome has occurred in that costs have escalated to a level not thought possible a few years ago. AngloGold has found itself in a position where it has sold 10 million ounces of gold forward at prices lower than the cost of production.

For every US\$1 increase in the gold price, the mark-to-market loss on the hedge book increases by US\$10 million. This seems fairly dire but it must be taken in context, as the same US\$1 increase in the gold price means the potential profits on

AngloGold's 63 million ounces of unhedged reserves increase by US\$63 million. The 10 million ounces of hedged production is only 13% of AngloGold's total reserves.

Most of the hedged ounces fall due within the next four years. The effect is that the medium-term earnings and cash flow will be depressed as the company delivers the low-priced ounces into the hedge. Thereafter, profits should increase markedly as the received price increases. Most investors are unwilling to wait four years and want to participate in the gold price upside now. Delivering the committed hedges over the next four years will result in the company being cash constrained and thus without the financial ability to invest in new growth projects.

"This could transform the business ... to one with the financial flexibility ... and deliver value to shareholders."

For these reasons, management has decided to reduce the hedge exposure. To achieve this AngloGold is raising R13.5bn through a rights offer. The funds raised will allow the company to reduce the hedge to 6.25 million ounces and invest in growth and exploration projects, further enhancing the value of the business. Post 2008 cash flows will be enhanced through greater spot deliveries. These cash flows could be invested in further hedge book reductions. This could transform the business from one that is hamstrung by the hedge to one with the financial flexibility to take advantage of opportunities and deliver value to shareholders.

AngloGold is our preferred gold investment and, by the time of going to print, our client portfolios' exposure to AngloGold will have increased further as a consequence of subscribing to the rights offer.



Delphine Govender

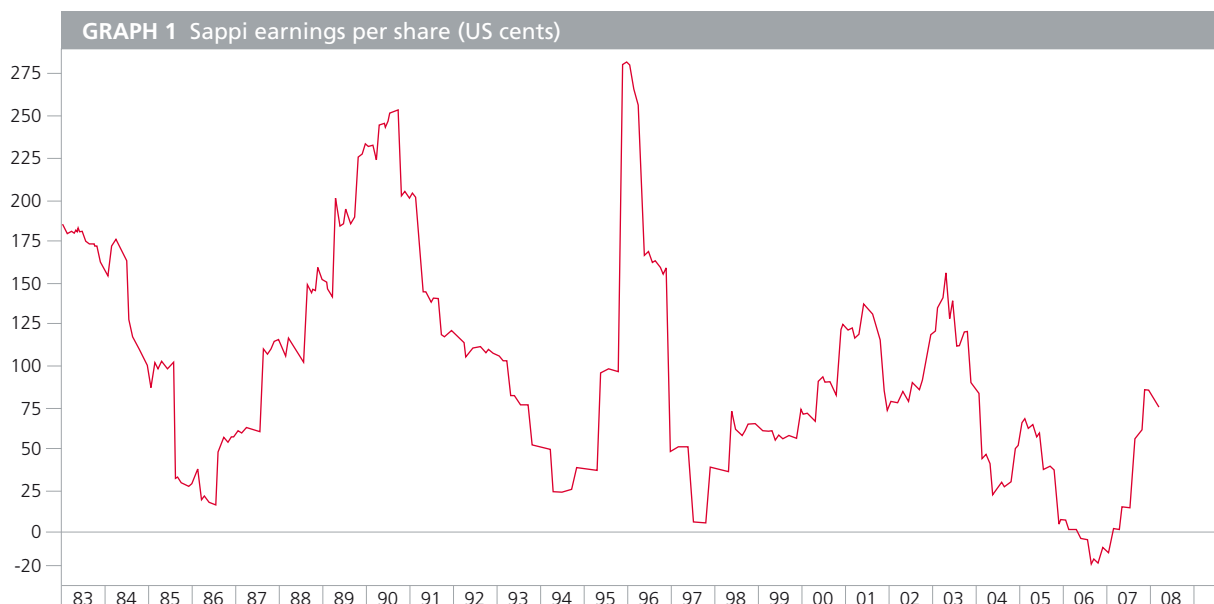
SAPPI - FROGS CAN MAKE GOOD INVESTMENTS, NOT ONLY PRINCES

EXECUTIVE SUMMARY: Based on its inconsistent track record, Sappi would not typify a 'high quality' company. However, investors who believe only historically 'good' companies make good investments will miss several opportunities to earn substantial returns. Delphine Govender explains why Allan Gray believes the stage is set for Sappi's earnings to return to more normal levels.

It is obviously much easier explaining to clients the investment case and merits of companies which have solid and consistent track records of profitability and operating performance – companies we have written about recently, such as Richemont, BAT and SABMiller, spring to mind as examples of this. Where companies have unique competitive advantages or have outstanding growth prospects and/or operate in industries with equally exciting growth opportunities, describing the rationale for these investments is also a relatively undemanding exercise. A company like MTN, one of our largest investments, is a good case in point. This is assuming, of course, that ultimately what makes these 'good' companies compelling investments for our clients is that they can be bought at what we assess to be attractive prices compared to what we think they are worth.

This does not preclude us, however, from investing in companies where the earnings history is massively cyclical and volatile; where the near-term earnings outlook is somewhat unpredictable; and/or which operate in industries or sectors where the prospects are sometimes opaque and possibly even dubious. Sappi is currently one such investment. In the current global business environment, where overall corporate profitability is very high, it is actually unusual to find a company where earnings are below normal levels.

Sappi is the world's largest producer of coated fine paper (also known as coated woodfree paper) and chemical cellulose. Coated fine paper is used in various printing mediums, but its main use is in glossy magazines and catalogues. Chemical cellulose (also called dissolving pulp) is used principally in the



Source: I-Net

production of viscose fabric and also in several consumer and pharmaceutical products.

Over the past 25 years Sappi has had a highly cyclical earnings history, achieving super-profits in one year, only to have earnings fall significantly a few years later. This earnings pattern has repeated itself over this period in varying degrees. See **Graph 1** on page 9.

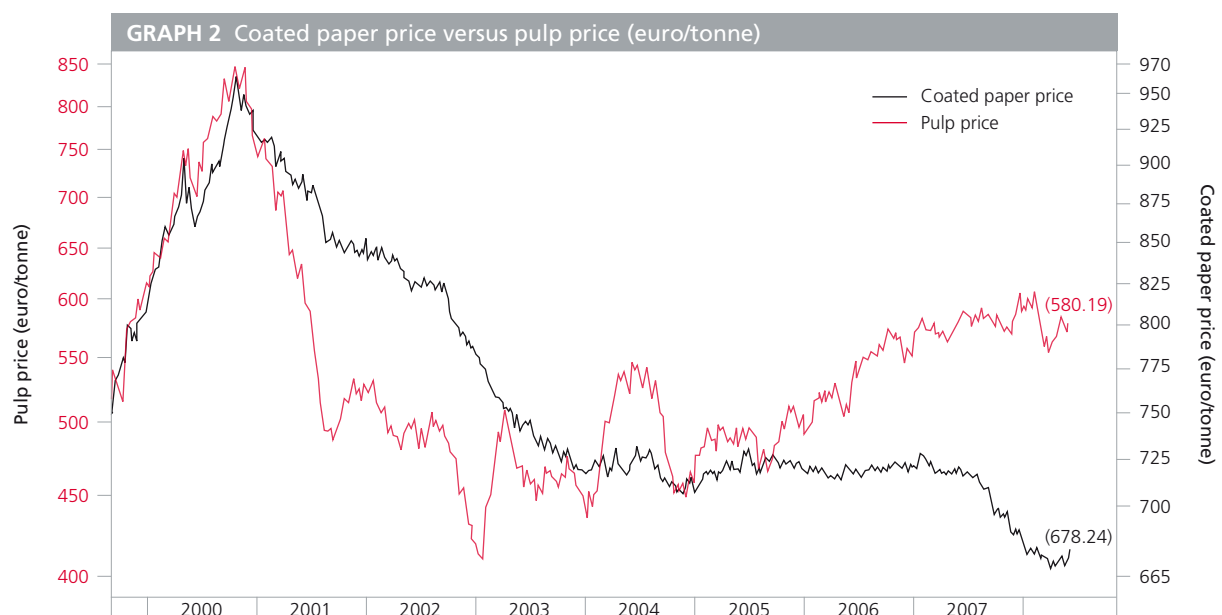
What drives Sappi's earnings?

For most commodity-producing companies, it is the price of the commodity that is usually the single biggest driver of revenue and earnings. Sappi's case is no exception - the coated woodfree paper price is the most important factor in driving profitability. The rand/dollar exchange rate is a further key driver. Sappi is geared to a weaker rand due to the high proportion of earnings that comes from outside South Africa, as well as the export component of its South African operations.

Despite the actual product of coated woodfree paper being quite similar across regions, the coated paper price differs from region to region. Meanwhile, the different regional prices do not necessarily move in tandem, owing to the costs and difficulties of transporting large volumes of paper.

The biggest reason for Sappi's current below-normal earnings has been the weak European coated paper price. Europe represents close to 60% of Sappi's coated paper sales and European coated paper prices have declined for over seven years. See **Graph 2** (black line - right hand side axis).

Overcapacity as a result of a fragmented supply side has been the primary reason for the lack of pricing power in Europe. To compound the challenging European pricing situation, a strong euro versus US dollar has significantly reduced the profitability of European coated paper exports, more than half of which go to the United States. Further pressure has come from an increasing pulp price (red line in Graph 2) with no concomitant increase in the paper price. With pulp being



Source: I-Net

the largest input cost in the manufacturing of paper, this disconnect in the price of pulp versus the price of paper has caused a considerable squeeze to the operating margins of the paper manufacturers.

Therefore, the most important catalyst for a full recovery in Sappi's earnings will be consolidation among the main coated paper producers in Europe, with effective and material capacity rationalisation and pricing power as the end goal. While betting on consolidation might ordinarily seem very brave, given the prolonged period of dismal returns for all players, the balance of probability now distinctly lies in this occurring sooner rather than later. One of the key supporting factors is that almost without exception the management teams at the helm of the various major European paper companies have been in place for less than three years. These newer teams tend to be less emotionally attached to assets (which they will need to rationalise/close) and also more impatient to see change.

While a recovery in European coated paper prices would have a dramatic impact on Sappi's earnings, it would be remiss to ignore other key aspects of the overall business, which also underpin earnings. These include:

- The performance of Sappi's North American coated paper business, which has been steadily improving over the past three years. Ironically, about three to five years ago, the North American coated paper market resembled the European coated paper market today. United States coated paper manufacturers have been consolidating

(the top three producers now account for almost 70% of the market) and cutting capacity, and this has enabled meaningful price increases. We expect the North American operation to continue its steady improvement.

- The chemical cellulose operation in South Africa, which commands a leading global market share position. The demand growth of this segment is outpacing the more mature pulp and paper grades. Wisely, Sappi has been expanding capacity in this operation which will ensure the group retains its dominant global market share. This expanded operation is expected to contribute meaningfully to group profits once it is fully up-and-running. Chemical cellulose also provides the group with a hedge in that its end uses are on the increase, which could counteract the ongoing threat that electronic media presents to the coated paper market.

Based on its inconsistent profitability track record, Sappi would not exemplify a typical high quality company. However, investors who believe only historically 'good' companies make good investments will miss several opportunities to earn substantial returns. We believe the stage is set for Sappi's earnings to return to more normal levels. While the timing of this earnings recovery might depend on a few material events occurring, when these events eventually do occur, the impact on Sappi will be significant, and the returns will be solid. This will illustrate that, in investments, uncovering companies that deliver princely returns is not only about those which have achieved eminence, but also about those with unlikely potential.

"Over the past 25 years, Sappi has had a highly cyclical earnings history,"



Matthys de Kock

HISTORY RHYMING? PRICE DISPARITIES TYPICALLY REVERSE THEMSELVES

EXECUTIVE SUMMARY: Over time, every company and each sector of the stockmarket oscillate between seasons of outperformance and seasons of underperformance. Matthys de Kock notes that the tendency for Allan Gray's share portfolio has been to underperform the FTSE/JSE All Share Index (ALSI) in times when the relative prices of the major sectors move to extremes. This is the case at present. The good news, however, is that, once the disparities have narrowed, outperformance is likely to follow.

Past performance is never an indication of future return. However, in many instances history can be instructive. In the words of Mark Twain, 'while history may not repeat itself, it does occasionally rhyme'. A rhyme or pattern that we have observed is the tendency of our share portfolio to underperform the ALSI during periods when prices of the major sectors move to extremes relative to one another. While the duration of each period of past underperformance varied, clients will be happy to know that, once disparity narrowed, underperformance gave way to outperformance.

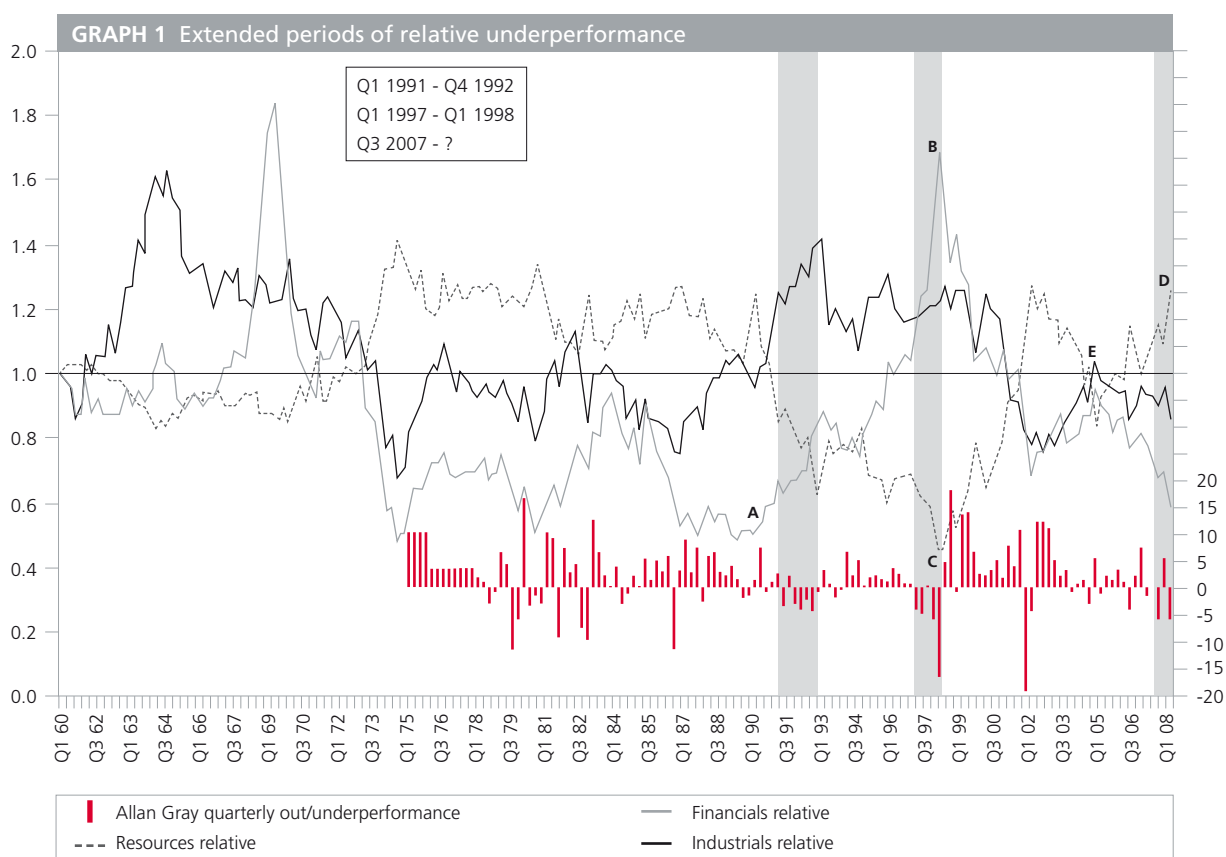
Graph 1 represents the long-term relative performance of the three major sectors that comprise the ALSI, namely resources, industrials and financials. For readers not familiar with relative strength, a rising line indicates outperformance by a specific sector of the overall market, whereas a declining line signifies a period of relative underperformance. While the fortunes of each sector have varied much over time, it is notable that periods of out- or underperformance have never been sustained indefinitely. The market correction in the third quarter of 1998 brought an end to the extraordinary run of outperformance by financials that characterised most of the 1990s (**Points A to B**, grey line). Meanwhile the seemingly perennial underperformance of resources during the 1980s until the late 1990s eventually gave way to a commodity bull market that continues to rage to this day (**Points C to D**, dotted line). Over time each sector has alternated between seasons of outperformance and underperformance as profits are continuously redistributed among economic participants and investors bid the prices of these companies up and/or down.

"It is during these subsequent periods of narrowing disparities that our portfolios have delivered meaningful outperformance."

The red bar also on Graph 1 represents the quarterly out/underperformance of Allan Gray's share portfolio compared to that of the ALSI since the inception of the firm in 1974. While readers may be familiar with our long-term track record of outperformance, the inconsistency of outperformance over the short term may come as a bit of a surprise. Long-term outperformance does not come in a straight line. The inherent variability in short-term performance presents a compelling argument as to why performance evaluation is more meaningful over longer periods of time. Many investors have missed out on satisfactory long-term returns due to a focus on short-term results.

In the past, disparities in relative market prices significantly influenced the magnitude of our relative performance. The three shaded areas in the graph indicate periods where the disparity in relative pricing among sectors widened considerably for an extended time. During these periods, Allan Gray's equity portfolios delivered short-term performance well below that of the overall market as can be seen from observing the bar chart. Our spells of underperformance generally persisted until the trend in relative performance reversed. It is during these subsequent periods of narrowing disparities that our portfolios have delivered meaningful outperformance.

The relevance of these past occurrences is that we are currently witnessing a significant widening of relative price disparity in the South African stockmarket that is contributing yet again to short-term underperformance. In a mere 24 months relative price parity at a sector level (**Point E**) has given way to significant levels of disparity.



Source: Allan Gray research

Over this period resources have outperformed the market return by 21%, whereas the relative position of industrials remained largely unchanged and financials have declined on a relative basis by close to 40%. Put simply, over the last two years, an investment in financials yielded only 60% of the market's return whereas an investment in resources would have left an investor with 20% more than the market and double the amount invested in financials.

The current dispersion in relative returns at a sector level is not too dissimilar from conditions in 1998 when the market's infatuation with IT stocks, banks and niche financial service companies drove the prices of these stocks to irrationally

high levels, while resources were shunned. The market seems to have come full circle, yet this time around the former laggards (commodities and construction) are leading the outperformance charge, while financials and technology are faltering.

Our equity portfolios tend to underperform when relative prices move towards extremes as a result of our investment philosophy. Allan Gray's philosophy is directed at identifying and exploiting discrepancies between the price the market is willing to pay for a company and its underlying intrinsic value. Through a rigorous fundamental process we try to identify companies that can be acquired at a price below intrinsic value

while at the same time avoiding shares where price exceeds fair value. As we are not concerned with a share's weighting in the benchmark, our portfolio is generally overweight in shares we deem attractive (underpriced) and we avoid shares we deem unattractive (overpriced). The result is a portfolio that differs markedly from the benchmark, which ultimately translates into different performance.

It is important to note that there is no rule that prohibits the prices of those shares that we consider attractive, and hence purchase, from declining even further. Conversely, nothing prevents the prices of shares that we deem overpriced – and therefore do not hold – from rising even further. Market prices are completely oblivious to our investment strategy and more attuned to the prevailing sentiment. It is under these conditions – when market sentiment drives the prices of shares we deem cheap and own lower, and at the same time, the prices of companies we deem expensive and don't own even higher – that our

selection of shares delivers returns lower than those of the market. At present Allan Gray's overweight position in underperforming financials and industrials along with our underweight position in outperforming resources is injecting an unwelcome dose of short-term underperformance into our clients' portfolios.

“In the words of Mark Twain, ‘while history may not repeat itself, it does occasionally rhyme’.”

While we never welcome it, we are rarely concerned with bouts of underperformance, especially when this is a consequence of our investment philosophy. History shows that periods of widening disparities have never persisted indefinitely and are often followed by rather sudden and sharp

reversals back to parity.

So, like Mr Twain, we look forward to the market's occasional rhyming as it provides an opportunity to deliver long-term outperformance to our clients' portfolios.



Chris du Toit

THE STABLE MEDICAL PORTFOLIO - FOUR YEARS LATER

EXECUTIVE SUMMARY: Allan Gray's Stable Medical Portfolio was launched four years ago to encourage medical schemes to take advantage of the Medical Schemes Act, which permits them to invest up to 40% of their assets in equities. Chris du Toit notes that the Portfolio has returned no less than 16.7% per annum (before deducting investment management fees). While the Portfolio's exposure to equities has been reduced from around 30% to 22.3%, he believes that the Portfolio will continue to provide an attractive opportunity for schemes to benefit from the upside of equity markets, and still meet their shorter-term capital protection needs.

Allan Gray launched the Stable Medical Portfolio in 2004 for medical schemes wanting to invest in a portfolio that complied with the Medical Schemes Act. Traditionally, most medical schemes invested the bulk of their assets in low-risk cash and money market instruments. However, the asset class regulations in the Act allow schemes to invest up to 40% of their assets in equities. We saw the Stable Medical Portfolio as an opportunity for schemes to gain exposure to equities and other 'risky' asset classes, in order to grow their assets in real terms, and at the same time comply with the regulations of the Act.

This is a balanced portfolio, with Allan Gray actively managing the equity exposure as well as equity selection, according to the same bottom-up fundamental investment philosophy and process that we follow in managing all our clients' assets. Advantages of the Stable Medical Portfolio include:

- Investment into assets other than cash, allowing schemes to earn a superior return on their assets over time
- Low volatility of returns and a low risk of losing capital
- Compliance with the asset class restrictions of the Medical Schemes Act

The Portfolio's benchmarks are the choice of the return on the 3-month cash deposit index + 2% or CPI + 3% (see **Table 1**).

Returns and risk

The Portfolio returned 16.7% per annum (before deducting investment management fees) from 1 May 2004 to 30 June 2008. This is an outperformance of 7% versus CPI + 3% and an outperformance of 6.2% versus cash + 2%.

The reason for this exceptional return was the phenomenal return from South African shares during this time. The FTSE/JSE All Share Index (ALSI) returned 32.9% per annum over the period and Allan Gray's Equity Portfolio (which mirrors very closely the equity portion of the Stable Medical Portfolio) returned 34.3% per annum over the same period.

This significant return above the benchmark is certainly not sustainable over the long term and we expect the Portfolio to deliver returns closer to its benchmark over time. Based on the very long-term relationships between inflation and asset class returns, a portfolio like this (with an equity exposure in the region of 30%) would have returned around 3% above inflation over the long term.

TABLE 1 Portfolio returns to 30 June 2008

	Stable Medical Portfolio	CPI + 3%	Cash + 2%
6 months	1.0	8.9	6.5
1 year	7.0	15.4	12.8
3 years (annualised)	15.7	11.2	10.8
Since inception (annualised)	16.7	9.7	10.5

Source: Allan Gray research

Medical schemes are different from traditional pension funds in that they need access to their capital at very short notice in order to meet claim payments from their members. This is one of the reasons why schemes can invest only 40% in equities. Given the short-term volatility that equities experience, schemes cannot run the risk that a large portion of their assets may experience negative returns just as they need to withdraw capital.

Through Allan Gray's equity selection and asset allocation process, the Portfolio has benefited from the outperformance of equities and has experienced low volatility of returns over short periods of time. The largest monthly decline for the Portfolio has been -2.0% experienced in June 2008, on the back of a 4.4% decline in the ALSI.

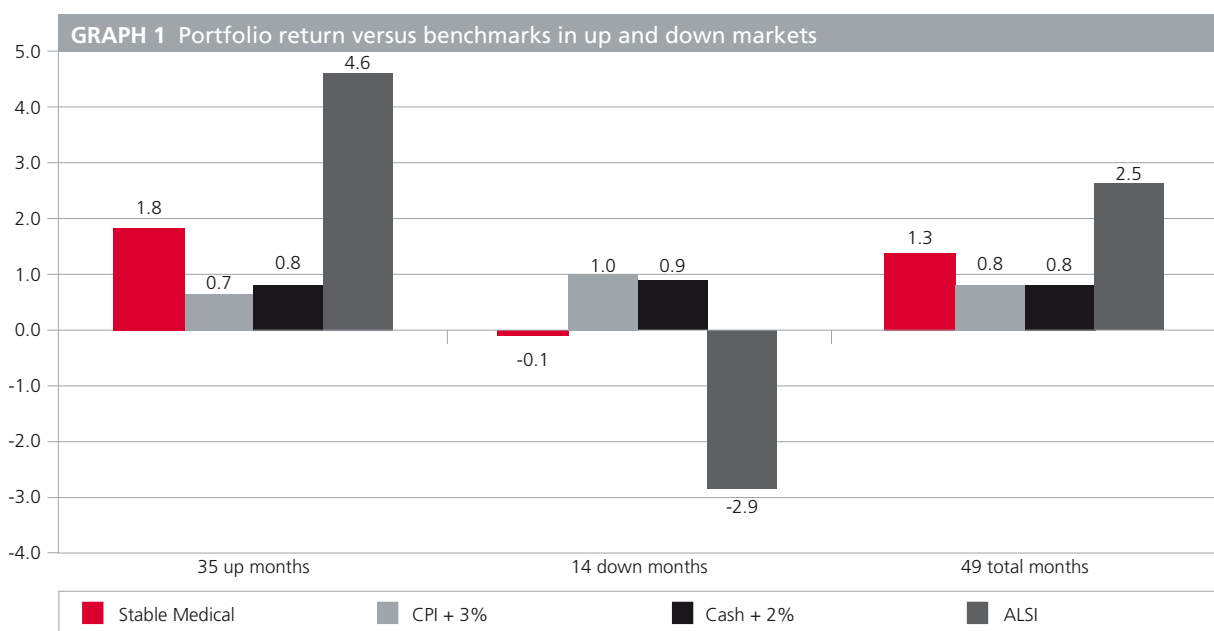
Graph 1 is one way of analysing how effective the Portfolio has been in avoiding negative returns from equities, while still managing to benefit when equities outperform. The graph summarises the return of the Portfolio versus its

benchmarks and the ALSI, where the returns of the Portfolio and benchmarks have been categorised according to whether the equity market had positive or negative returns.

During months where the market was up, the ALSI returned 4.6% per month on average. The Stable Medical Portfolio participated in this upside, returning 1.8% per month on average. During months where markets were down, the ALSI lost an average of 2.9% per month. Through asset allocation and stock selection, the Stable Medical Portfolio managed to preserve capital (on average) during these negative months.

Table 2 compares the risk-adjusted performance of the Portfolio versus its benchmarks. We also provide statistics for the ALSI and All Bond Index (ALBI) for comparative purposes. The volatility of the Portfolio at 4.7% per annum is very low compared with both equities and bonds.

A downside volatility of only 3.3% per annum for the Portfolio indicates that a substantial amount of the 4.7%



Source: Allan Gray research

TABLE 2 Portfolio risk statistics versus benchmarks

	Stable Medical Portfolio	CPI + 3%	Cash + 2%	All Share Index	All Bond Index
Annualised volatility	4.7	1.6	0.4	15.0	5.7
Sharpe ratio	1.8	-	-	1.6	-0.2
Downside volatility	3.3	-	-	11.3	3.4

Source: Allan Gray research

volatility in returns was attributable to positive returns above its mean, a source of 'risk' with which most investors would be very comfortable. The Sharpe ratio of 1.8 indicates that the Portfolio outperformed cash by 1.8% for every 1% of volatility in returns. This compares favourably with the ALSI, which had a Sharpe ratio of 1.6.

Current strategy of the Portfolio

Given the exceptional returns from South African shares over the last four years, we have reduced the Portfolio's exposure to equities. Currently, the Portfolio has 22.3% net equity exposure, well below the maximum allowable 40%. The shares we find attractive include MTN, Remgro, Richemont and SABMiller – all large, high-quality companies with globally diversified businesses and less cyclical demand patterns for their products. We believe they will be able to grow their earnings faster than inflation over time (see **Table 3**).

Some 15% of the Portfolio is exposed to hedged equities. This portion of the Portfolio uses ALSI 40 futures contracts to eliminate exposure to the stockmarket in favour of a cash-like return, whilst still being exposed to any outperformance

TABLE 3 Asset allocation at 30 June 2008

Net equities	22.3
Listed property	2.0
Newgold	4.5
Fixed interest	56.2
Hedged equities	15.0
Total	100.0

Source: Allan Gray research

by our selection of shares. We view this as an attractive alternative to cash and bonds, especially given the increased opportunities we see for positive relative performance of our shares versus the market.

The fixed interest assets are invested in short-duration money market instruments, providing an attractive yield and acting as a buffer against volatile returns from equities. The duration of the fixed interest assets is a low 51 days.

Compliance with regulation and liquidity

The Portfolio continues to be managed in compliance with the asset class restrictions of the Medical Schemes Act. The Portfolio is priced and trades daily, allowing for quick access to funds if necessary.

We are certainly happy with the performance of the Portfolio since its inception but again caution investors not to expect the returns of the past four years to be repeated. We believe that by consistently applying our investment philosophy, the Portfolio will provide an attractive opportunity for schemes to benefit from the upside in equity markets, while still meeting their shorter-term capital protection needs.



Craig Bodenstab

Jonathan Brodie

STAYING THE COURSE THROUGH TESTING TIMES

EXECUTIVE SUMMARY: In these testing times for global investors, Craig Bodenstab and Jonathan Brodie articulate the contrarian investment philosophy long practised at Orbis, Allan Gray's global asset management partner. While successful implementation of this philosophy has generated attractive long-term returns, the strategy has also entailed periods of below-average performance. An understanding of the philosophy, and the fact that the adverse periods are an inherently unpredictable part of the approach, will hopefully give investors the confidence to stay the course and ultimately benefit over the longer term.

Global markets have experienced turbulent conditions recently, with the media reporting on each development in near-sensational tones. How should the investor best make long-term decisions in the face of such challenging news and noise?

An understanding of the philosophy underpinning the investment manager's strategies is essential

Without this, the investor is prone to the all-too-well documented occupation of buying high and selling low. Therefore, we thought it worthwhile to articulate our investment philosophy so that investors can fully understand our investment performance over time, including the inevitable periods of future underperformance. The investment approach of Orbis, like that of Allan Gray, focuses overwhelmingly on analysing individual businesses. We build portfolios by picking shares in companies that offer the prospect of above-average long-term returns with lower risk of permanent capital loss. The underlying philosophy is that, while stockmarket prices are the best indicator of value for companies over long time periods, substantial deviations can occur over the short to medium term. **Graph 1** illustrates our contrarian investment approach.

The intrinsic value of a particular company

Represented by the shaded blue line, this is the most significant element of the graph. Intrinsic value is the discounted value of the profits which the business could pay out over its life. The majority of our analysts' time and effort is spent on this aspect. There are two other noteworthy features on this graph. Firstly, time is measured in years, not months or days because

intrinsic value must encompass a longer-term view to yield meaningful results. Secondly, the intrinsic value line is fuzzy because even its most sophisticated calculation is an estimate given the numerous assumptions required to determine a company's worth.

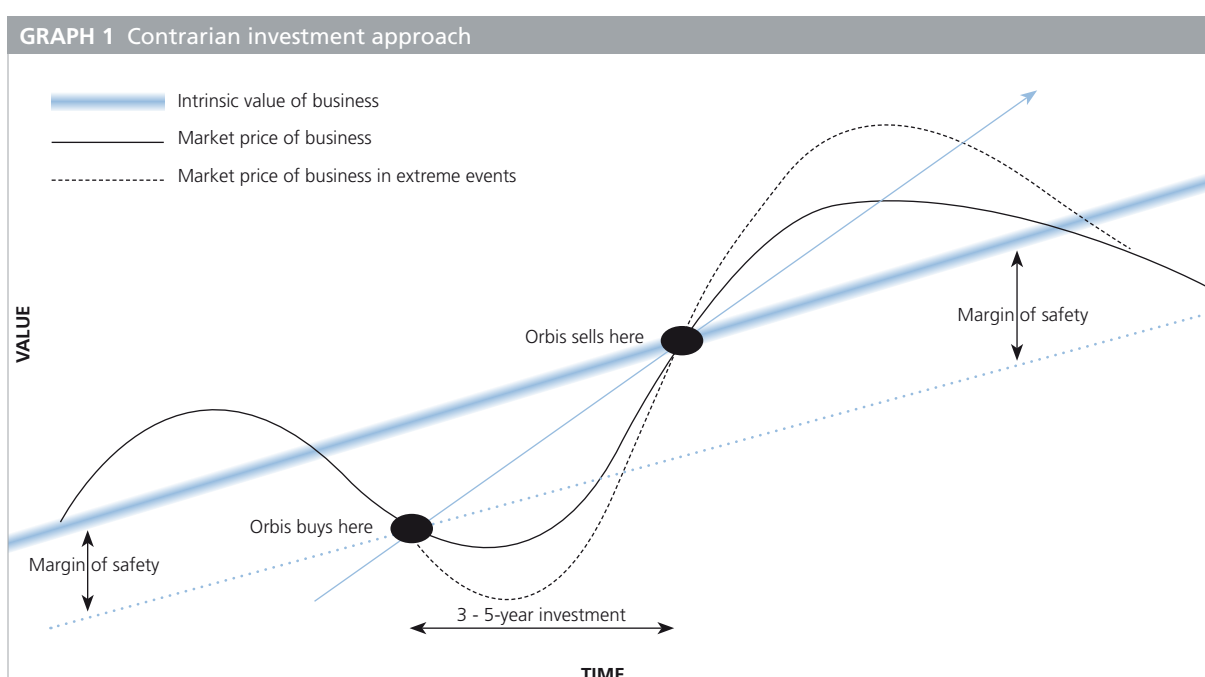
Stock price

The solid black line represents the stock price. The shares of companies we buy are publicly traded. Whereas intrinsic value is somewhat imprecise, it is relatively stable, adjusting in line with the long-term profitability of the company. Not so the readily observable stock price. In our opinion, short-term market price change is driven more by emotional factors than by the long-term intrinsic worth of a business. In practice, stock prices tend to oscillate around intrinsic value, sometimes deviating but generally being driven back towards the fundamental value which becomes evident over time.

Margin of safety

Opportunities arise when we find companies trading below intrinsic value. Very important is the dotted line below the intrinsic value band, representing our margin of safety. Because our assessment of intrinsic value is necessarily imprecise, we buy the shares only if they are trading meaningfully below that assessment (the 'Orbis buys here' circle). The margin of safety provides a buffer against potential losses as a result of an inaccurate assessment of a business' worth.

Over time the areas of the market where we find this margin of safety vary. Sometimes we are able to buy 'average' companies at very low prices, and at other times we can buy



Source: Orbis

‘great’ companies at average prices. Whether they are large cap or small cap companies, growth or value stocks, our discipline remains the same. We search out great investments – which depend, critically, on the ability to buy them below intrinsic value.

When we are correct, generally the market re-prices the stock towards (or beyond) intrinsic value. The arrow drawn through the ‘Orbis buys here’ and the ‘Orbis sells here’ points slopes upwards more steeply than the intrinsic value line itself. Our long-term outperformance results from our research

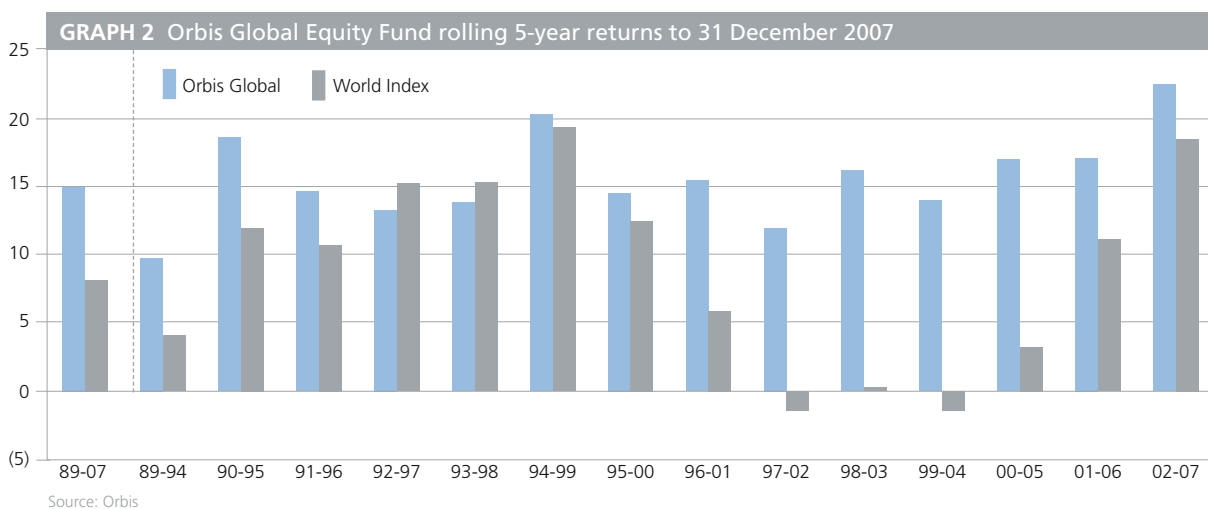
methodology being able to identify a more attractive portfolio than the market offers as a whole.

Two broad reasons why we may experience a period of underperformance

Firstly, we may be wrong. The ‘Orbis buys here’ point lies well below our assessment of intrinsic value. By definition, this is a contrarian position as we are positing that the stockmarket price is ‘wrong’. Despite our work, we make mistakes.

“I met hundreds of investment managers pitching their services to Harvard. The process confirmed to me that very few firms have made the effort to hardwire a disciplined secular process that identifies new opportunities and reduces the risk of being sucked into crowded trades at the wrong time.”

Mohamed El-Erian, Co-CEO and Co-CIO of Pimco, former President and CEO of Harvard Management Company (HMC).
Quote taken from Pimco’s Secular Outlook 2008.



Secondly, we often buy and sell too early. Even when our analysis is correct, market sentiment often drives prices beyond our buy or sell points.

A reason why other managers may not invest in this way

The discomfort of short-term under-performance can be so great that career risk and/or compensation structures push investment managers to seek short-term profit through an immediate transaction instead of long-term profit from appreciated value. The source of their intended profit comes solely from an expectation of selling to someone else at a higher price in the relatively near future.

Benefits in terms of risk

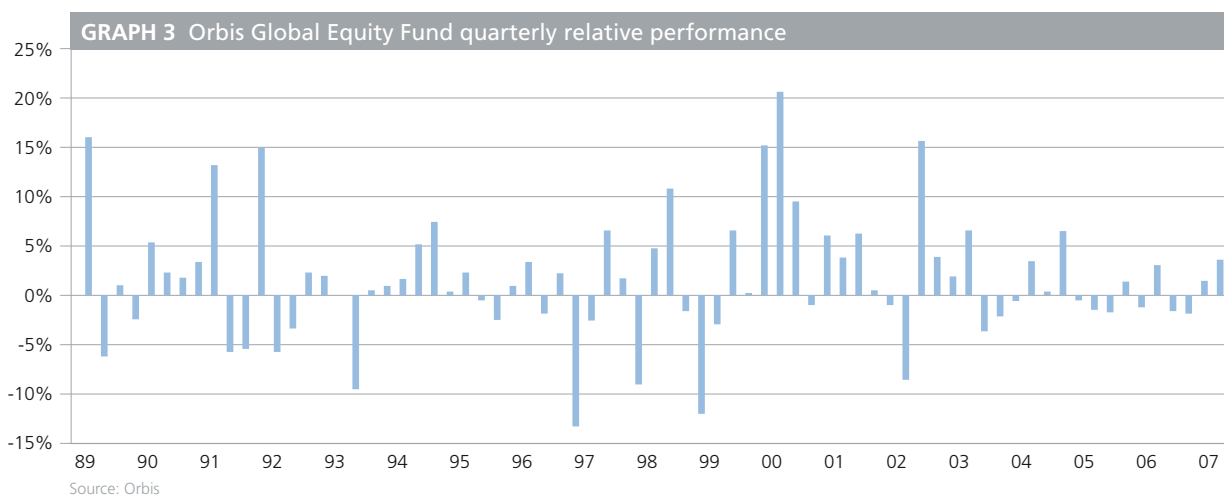
We define risk as the permanent impairment of our clients' capital. In other words, we do not like to lose money. Since inception, our Funds' worst drawdown (Global Fund) has been 29%, not insubstantial, but lower than the 47% experienced

by the World Index. Moreover, our recovery time has averaged about five months compared to 18 months for the Index. The lower loss and quicker recovery should be intuitive as we aim to invest with a margin of safety and benefit from the tendency of prices to move back to intrinsic value.

"Since inception, the Global Fund has delivered an annualised return of 14.7% versus 7.9% for the World Index."

Graph 2 shows returns since inception, separating returns for the Orbis Global Equity Fund into five-year rolling return periods measured against the World Index. Five years is consistent with our investment horizon and therefore the minimum investment period we would recommend for prospective clients.

Since inception, the Global Fund has delivered an annualised return of 14.7% versus 7.9% for the World Index. Looking at the rolling five-year periods, in absolute terms, returns have been positive, in excess of 10% per annum with the exception of 1989-1994 when they were slightly below this. Relative to the index, we outperformed in every period except those ending during the late 1990s when we lagged the momentum market of the time.



However, the long-term return picture would not be complete without showing the quarterly relative returns over the same period.

The pattern of our short-term relative returns is anything but smooth

A cursory glance shows that our quarterly relative performance is volatile and frequently negative. Our philosophy entails understanding as much as we can about the value of the underlying companies, whereas short-term performance is dominated by stockmarket price changes, a factor well

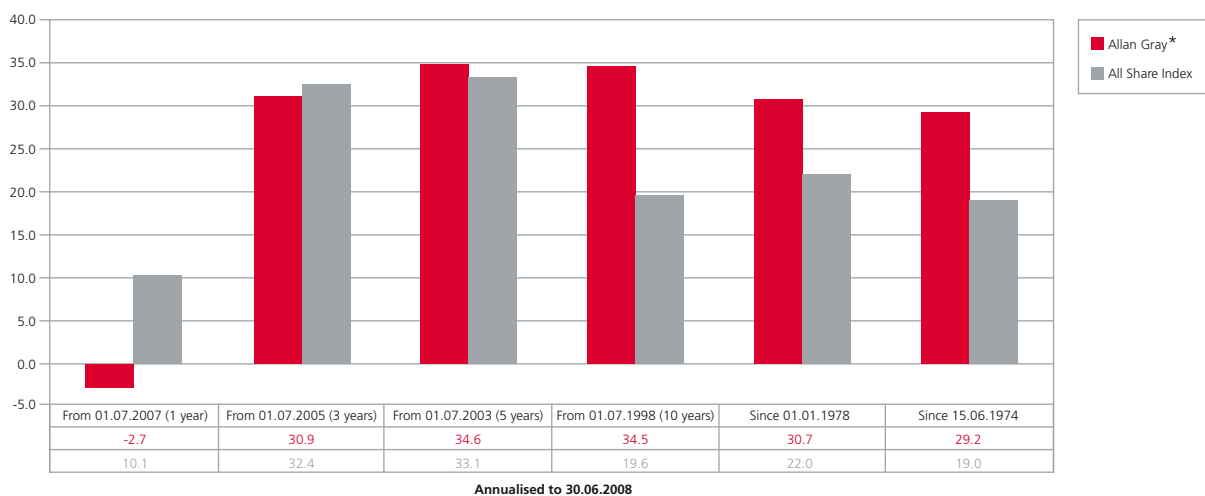
beyond our control. We simply accept the 'risk' of short-term underperformance and recognise that our alpha (outperformance) does not come in a straight line.

While we continue to believe that our philosophy is sound and sustainable, we are mindful that a challenge to this philosophy is the possibility – if not the certainty – of periods of short-term underperformance. We hope that this explanation of our investment strategy will provide investors with the confidence to downplay short-term developments and the fortitude to use our Funds effectively in securing their long-term financial goals.

Investment track record

Allan Gray Limited Global Mandate Share Returns vs. FTSE/JSE All Share Index

Period	Allan Gray*	FTSE/JSE All Share Index	Out/Underperformance
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 (to 30.06)	-6.0	6.4	-12.4
Annualised to 30.06.2008			
From 01.07.2007 (1 year)	-2.7	10.1	-12.8
From 01.07.2005 (3 years)	30.9	32.4	-1.5
From 01.07.2003 (5 years)	34.6	33.1	1.5
From 01.07.1998 (10 years)	34.5	19.6	14.9
Since 01.01.1978	30.7	22.0	8.7
Since 15.06.1974	29.2	19.0	10.2
Average outperformance			10.2
No. of calendar years outperformed			26
No. of calendar years underperformed			7



* Note: Allan Gray commenced managing pension funds on 01.01.1978. The returns prior to 01.01.1978 are of individuals managed by Allan Gray, and these returns exclude income.

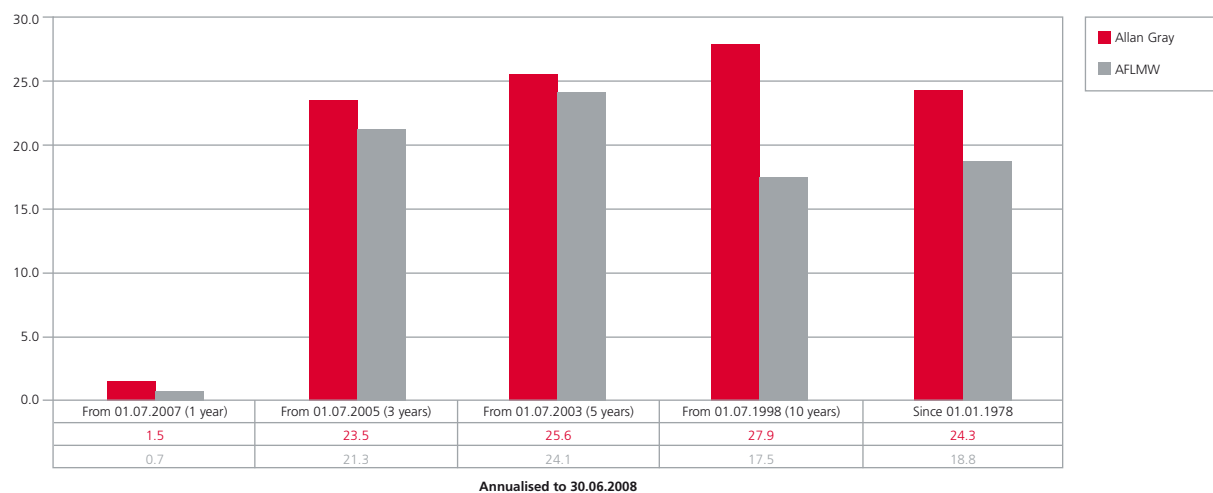
Note: Listed property included from 1 July 2002.

An investment of R10 000 made with Allan Gray on 15 June 1974 would have grown to **R61 404 318** by 30 June 2008. By comparison, the returns generated by the FTSE/JSE All Share Index over the same period would have grown a similar investment to **R3 744 885**.

Investment track record

Allan Gray Limited Global Mandate Total Returns vs. Alexander Forbes Global Manager Watch

Period	Allan Gray	AFLMW**	Out/Underperformance
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 (to 30.06)	-1.7	-2.5	0.8
Annualised to 30.06.08			
From 01.07.2007 (1 year)	1.5	0.7	0.8
From 01.07.2005 (3 years)	23.5	21.3	2.2
From 01.07.2003 (5 years)	25.6	24.1	1.5
From 01.07.1998 (10 years)	27.9	17.5	10.4
Since 01.01.1978	24.3	18.8	5.5
Average outperformance			5.5
No. of calendar years outperformed			24
No. of calendar years underperformed			6



** Consulting Actuaries Survey returns used up to December 1997. The return for June 2008 is an estimate.

An investment of R10 000 made with Allan Gray on 1 January 1978 would have grown to **R7 532 056** by 30 June 2008. The average total performance of global mandates of large managers over the same period would have grown a similar investment to **R1 891 575**.

Allan Gray annualised performance in percentage per annum to 30 June 2008

	SECOND QUARTER (unannualised)	1 YEAR
UNIT TRUSTS**		
EQUITY FUND (AGEF) FTSE/JSE All Share Index	***	-1.1 10.1
BALANCED FUND (AGBF) Average of both Prudential Medium Equity category and Prudential Variable Equity category (excl. AGBF)	***	0.4 0.7
STABLE FUND (AGSF) - (NET OF TAX) After-tax return of call deposits plus two percentage points (Net of tax)	***	5.6 8.8
STABLE FUND (AGSF) - (GROSS OF TAX) After-tax return of call deposits plus two percentage points (Gross of tax)	***	6.6 11.9
MONEY MARKET FUND (AGMF) Domestic fixed interest money market unit trust sector (excl. AGMF)	***	10.9 10.6
ORBIS GLOBAL FUND OF FUNDS (AGGF) **** 60% of the FTSE World Index and 40% of the JP Morgan Government Bond Index Global (rands)	***	10.9 12.3
OPTIMAL FUND (AGOF) Daily call rate of Firstrand Bank Ltd	***	7.0 9.7
BOND FUND (AGBD) BEASSA All Bond Index (total return)	***	2.3 -2.7
ORBIS GLOBAL EQUITY FEEDER FUND (AGOE) FTSE World Index (rands)	***	-0.6 1.1
FOREIGN-ONLY (RANDS)**		
ORBIS GLOBAL EQUITY FUND (RANDS) FTSE World Index (rands)	-10.3 -5.1	-1.1 0.9
ORBIS JAPAN EQUITY (YEN) FUND (RANDS) Tokyo Stock Price Index (rands)	-9.5 -1.6	-0.9 -2.2
ORBIS OPTIMAL SA FUND-US\$ CLASS (RANDS) US\$ Bank Deposits (rands)	-6.9 -3.0	14.2 16.0
ORBIS ASIA EX-JAPAN EQUITY FUND (RANDS) MSCI Asia Ex-Japan (rands)	-9.5 -11.4	12.3 4.8
GLOBAL BALANCED MANDATE (RANDS) - FOREIGN COMPONENT 60% of the MSCI and 40% of the JP Morgan Government Bond Index Global (rands)	-9.1 -6.0	8.8 12.4
POOLED RETIREMENT FUNDS		
ALLAN GRAY LIFE GLOBAL BALANCED PORTFOLIO Mean of Alexander Forbes Global Large Manager Watch *	-3.9 -2.4	1.6 0.7
ALLAN GRAY LIFE DOMESTIC BALANCED PORTFOLIO Mean of Alexander Forbes Domestic Manager Watch *	-2.7 -2.0	-0.3 0.3
ALLAN GRAY LIFE DOMESTIC EQUITY PORTFOLIO FTSE/JSE All Share Index	-2.1 -3.4	-0.4 10.1
ALLAN GRAY LIFE DOMESTIC ABSOLUTE PORTFOLIO Mean of Alexander Forbes Domestic Manager Watch *	-1.8 -2.0	7.0 0.3
ALLAN GRAY LIFE DOMESTIC STABLE PORTFOLIO Alexander Forbes Three-Month Deposit Index plus 2%	-0.6 3.2	5.9 12.8
ALLAN GRAY LIFE FOREIGN PORTFOLIO ** 60% of the MSCI Index and 40% JP Morgan Global Government Bond Index	-8.7 -6.0	9.7 12.4
ALLAN GRAY LIFE DOMESTIC OPTIMAL PORTFOLIO ** Daily Call Rate of Nedcor Bank Limited	1.5 2.7	7.5 10.5
ALLAN GRAY LIFE GLOBAL ABSOLUTE PORTFOLIO Mean of Alexander Forbes Global Large Manager Watch *	-2.1 -2.4	9.4 0.7
ALLAN GRAY LIFE DOMESTIC MEDICAL SCHEME PORTFOLIO Consumer Price Index plus 3% p.a. *	-0.3 4.9	7.0 15.4
ALLAN GRAY LIFE GLOBAL STABLE PORTFOLIO Alexander Forbes Three-Month Deposit Index plus 2%	-0.7 3.2	8.9 12.8
ALLAN GRAY LIFE RELATIVE DOMESTIC EQUITY PORTFOLIO FTSE/JSE CAPI Index	0.5 1.8	6.3 7.5
ALLAN GRAY LIFE MONEY MARKET PORTFOLIO ** Alexander Forbes Three-Month Deposit Index	2.8 2.7	10.9 10.6
ALLAN GRAY LIFE ORBIS GLOBAL EQUITY PORTFOLIO ** FTSE World Index (rands)	-10.3 -5.2	-1.2 0.9
SEGREGATED RETIREMENT FUNDS		
GLOBAL BALANCED MANDATE Mean of Alexander Forbes Global Large Manager Watch # *	-3.8 -2.4	1.5 0.7
DOMESTIC BALANCED MANDATE Mean of Alexander Forbes Domestic Manager Watch *	-2.8 -2.0	-0.1 0.3
EQUITY-ONLY MANDATE FTSE/JSE All Share Index	-1.9 3.4	0.4 10.1
GLOBAL BALANCED NAMIBIAN HIGH FOREIGN MANDATE Mean of Alexander Forbes Namibia Average Manager *	-2.9 -2.4	6.1 4.1
EQUITY-ONLY RELATIVE MANDATE Weighted average of client specific benchmarks *	-0.9 -0.7	1.3 2.1

PERFORMANCE AS CALCULATED BY ALLAN GRAY.

Consulting Actuaries Survey returns used to 31 December 1997. Alexander Forbes Global Manager Watch used from 1 January 2006.

* The return for Quarter 2, 2008 is an estimate, as the relevant survey results have not yet been released.

** The returns and their respective benchmarks are net of investment management fees.

*** Unavailable due to ACI regulations.

**** As of 1 February 2004, the benchmark is displayed. The benchmark was the Morgan Stanley Capital International Index (in rands) prior to this date.

3 YEARS	5 YEARS	SINCE INCEPTION	ASSETS UNDER MANAGEMENT (R millions)	INCEPTION DATE
28.3 32.4	31.0 33.1	1790.5 690.9	16,908.7	01.10.98
20.7 18.8	24.2 21.9	556.9 275.5	24,216.0	01.10.99
13.4 7.2	14.0 7.0	198.3 82.6	20,997.6	01.07.00
14.2 9.7	15.0 9.4	227.4 123.1	20,997.6	01.07.00
8.8 8.6	8.5 8.4	86.8 86.8	6,549.3	03.07.01
16.0 14.9	- -	58.1 59.3	5,970.5	03.02.04
8.4 7.5	8.3 7.2	68.3 54.7	949.6	01.10.02
4.9 2.9	- -	29.2 22.5	48.5	01.10.04
16.6 16.5	- -	77.5 71.5	2,875.5	01.04.05
		Figures above unannualised		
17.4 16.5	17.4 14.6	21.0 14.1	15,616.1	01.01.90
9.4 12.6	11.9 13.0	16.4 9.0	6,802.3	01.01.98
11.9 10.4	- -	16.6 14.8	4,296.6	01.01.05
- -	- -	28.3 27.1	94.7	01.01.06
15.6 15.1	12.9 12.0	16.9 12.6	3,921.3	23.05.96
23.5 21.3	25.5 24.1	24.6 17.6	11,810.0	01.09.00
25.4 22.2	28.7 25.9	25.2 20.2	5,124.3	01.09.01
32.2 32.4	35.3 33.1	30.4 21.3	5,339.4	01.02.01
26.3 22.2	27.8 25.9	28.4 19.7	488.2	06.07.01
17.0 10.8	18.3 10.7	17.9 11.6	468.6	01.12.01
16.0 15.1	13.0 12.0	5.9 2.9	1,348.6	23.01.02
9.1 7.9	9.1 7.5	9.4 8.0	163.3	04.12.02
26.0 21.3	- -	24.6 22.6	837.5	01.03.04
15.7 11.2	- -	16.7 9.7	1,008.8	01.05.04
16.4 10.8	- -	18.2 10.5	2,466.7	15.07.04
32.2 31.0	33.7 32.7	35.2 33.9	496.2	05.05.03
8.8 8.6	8.9 8.5	9.8 9.5	572.8	21.09.00
17.1 16.5	- -	17.3 16.4	1,349.5	18.05.04
23.5 21.3	25.6 24.1	24.3 18.8	23,531.3	01.01.78
25.3 22.2	28.2 25.9	24.7 19.2	21,805.3	01.01.78
32.6 32.4	35.2 33.1	23.9 16.7	44,877.5	01.01.90
23.9 21.7	25.4 23.9	22.1 15.7	5,577.6	01.01.94
30.1 28.5	33.0 31.5	26.5 19.9	8,802.4	19.04.00

Balanced Fund Quarterly Disclosure as at 30 June 2008

	% of Fund
South African Equities	69.2
Resources	16.4
Anglogold Ashanti	4.8
Sasol	4.4
Harmony	3.7
African Rainbow Minerals	2.6
Positions individually less than 1% of total JSE listed securities held by the Fund	0.8
Financials	10.8
Sanlam	2.9
Standard Bank	2.8
ABSA	2.4
Firststrand	1.0
Positions individually less than 1% of total JSE listed securities held by the Fund	1.5
Industrials	41.7
SABMiller	6.9
Remgro	6.7
MTN	6.1
Richemont	5.2
Sappi	3.4
Shoprite	1.9
Nampak	1.5
Dimension Data	1.3
Sun International	1.2
Illovo Sugar	1.1
Mondi Ltd	0.9
Tiger Brands	0.7
Aspen Healthcare	0.7
Positions individually less than 1% of total JSE listed securities held by the Fund	4.1
Other Securities	0.4
Positions individually less than 1% of total JSE listed securities held by the Fund	0.4
Derivatives	-11.6
ALSI 40 09/08 - RMB	-11.6
---- Net South African Equities ----	57.6
Hedged South African Equities	11.6
Property	1.3
Liberty International	1.3
Commodities	2.4
New Gold ETF	2.4
Bonds	2.9
RSA Bonds	1.5
Corporate Bonds	1.4
Money-market and Call Deposits	9.8
Foreign Equities	7.0
Orbis Global Equity Fund	3.9
Orbis Japan Equity (Yen) Fund	2.9
Mondi PLC	0.2
Foreign Absolute Return Funds	7.4
Orbis Optimal SA Fund (US\$)	4.5
Orbis Optimal SA Fund Euro	3.0
Totals:	100.0

	Equity Fund	Balanced Fund	Stable Fund	Optimal Fund	Bond Fund	Money Market Fund	Global Fund of Funds	Global Equity Feeder Fund
Total Expense Ratio	2.90	1.87	1.85	1.63	0.83	0.30	2.20	2.90
Performance component	1.00	0.46	0.53	0.21	0.43	0.00	0.43	0.97
Fee at benchmark	1.71	1.17	1.16	1.14	0.29	0.29	1.22	1.45
Trading costs	0.17	0.18	0.10	0.23	0.00	0.00	0.20	0.16
Other expenses	0.02	0.06	0.06	0.05	0.11	0.01	0.35	0.32

A Total Expense Ratio (TER) of a portfolio is a measure of the portfolio's assets that was relinquished as a payment of services rendered in the management of the portfolio. This is expressed as a percentage of the average value of the portfolio, calculated for the year to the end of March 2008. Included in the TER is a proportion of costs that are 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, LIST, 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.



ALLAN GRAY LIMITED

Registration Number 2005/002576/06

Granger Bay Court Beach Road V&A Waterfront Cape Town 8001

P O Box 51318 V&A Waterfront Cape Town 8002 South Africa Tel +27 (0)21 415 2300 Fax +27 (0)21 415 2400

www.allangray.co.za info@allangray.co.za

ALLAN GRAY INVESTOR SERVICES

Portsworld Square Dock Road V&A Waterfront Cape Town 8001

Client Service Centre 0860 000 654 / +27 (0)21 415 2301

Client Service Email info@allangray.co.za

Client/IFA Service Facsimile 0860 000 655 / +27 (0)21 415 2492

IFA Service Centre 0860 000 653 / +27 (0)21 415 2690

IFA Email ifa@allangray.co.za

DIRECTORS

M Cooper B Bus Sc FIA FASSA **GW Fury** BA LLB MA CFA **DD Govender** B Com CA (SA) CFA

WB Gray B Com MBA CFA (Non-Executive) (Irish) **IS Liddle** B Bus Sc (Hons) CFA **SC Marais** PhD CFA (Non-Executive)

T Mhlambiso AB MBA JD (Non-Executive) **IN Mkhize** BSc MBA (Non-Executive)

COMPANY SECRETARY

CJ Hetherington B Com CA (SA)

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