PSG Equity Fund

Quarterly Portfolio Commentary as at 30 September 2018
by Shaun le Roux and Greg Hopkins

Current context

Emerging markets have underperformed dramatically in 2018, weighed down by rising US interest rates and turmoil in countries like Turkey and Argentina. This backdrop has seen the rand depreciate to the extent that it is trading weaker than it was before the ANC elective conference in December 2017. Domestic assets have suffered sharp declines this year.

We have also witnessed wide divergences in the performances of various global equity markets. The US stock market and economy have continued to perform strongly, with the S&P 500 returning 10.6% for the year to date. In contrast, the MSCI Emerging Markets Index has lost 7.7% and is approaching 20% declines from January highs. The FTSE/JSE All Share Index is down 3.8% year to date, and the FTSE/JSE Shareholder Weighted Index is 8% lower, extending the poor returns of the past four years.

Investor confidence in South Africa matches the gloomy economic backdrop and many domestic assets are trading at or near multi-year lows. Many well-owned stocks on the JSE, including the likes of Steinhoff, MTN, Aspen, Tiger Brands, Mediclinic and Woolworths, have disappointed in recent years and endured aggressive sell-offs. In most cases, starting valuations were high. We continue to avoid stocks that incorporate very high expectations, particularly when we consider how cheaply much of the market trades.

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. The prevailing fear in local markets has given rise to the opportunity to buy higher-quality stocks (particularly mid-cap industrials) at wide discounts to what we think they are worth.

Similarly, global stock markets are characterised by very wide divergences in valuations. This bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

Portfolio positioning

The fund retains healthy exposure to cheap domestic stocks. Due to the combination of low levels of earnings and bear market valuations, we expect excellent long-term returns from this component of the portfolio. Specifically, the fund has continued to add to its Old Mutual position after the unbundling of Quilter, partly funded by a selling of Nedbank. We perceive significant positive asymmetry at current share prices – very limited downside and healthy upside.

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate direct offshore exposure towards less crowded ideas in recent times. The global stocks the fund owns trade at healthy discounts to our assessments of intrinsic value. 31.6% of the fund is directly invested offshore.

We continue to avoid stocks that we perceive to be overpriced or where we consider risk to be too high. This has served our clients well in recent years: we have avoided many of the disappointing performers on the JSE as they did not meet the high bar we set for portfolio inclusion. While investing offers no guaranteed fail-safe, we believe that our insistence on a margin of safety places the odds in our clients' favour.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity	66.8%	Domestic equity	66.7%
Domestic property	1.4%	Domestic property	1.2%
Domestic cash	0.8%	Domestic cash	0.5%
Foreign equity	25.8%	Foreign equity	29.2%
Foreign property	5.0%	Foreign property	2.2%
Foreign cash	0.2%	Foreign cash	0.2

There may be slight differences in the totals due to rounding.

All data as per Bloomberg to 30 September 2018.

Disclaimer

Collective Investment Schemes in Securities (CIS) are generally medium to long-term investments. The value of participatory interests (units) or the investment may go down as well as up and past performance is not a guide to future performance. Fluctuations or movements in the exchange rates may cause the value of underlying international investments to go up or down. CIS are traded at ruling prices and can engage in borrowing and scrip lending. The Fund may borrow up to 10% of its market value to bridge insufficient liquidity. Where foreign securities are included in a portfolio, the portfolio is exposed to risks such as potential constraints on liquidity and the repatriation of funds, macroeconomic, political, foreign exchange, tax, settlement and potential limitations on the availability of market information. The portfolios may be capped at any time in order for them to be managed in accordance with their mandate. Excessive withdrawals from the portfolio may place the portfolio under liquidity pressures and in such circumstances a process of ring-fencing of withdrawal instructions and managed payouts over time may be followed. PSG Collective Investments (RF) Limited does not provide any guarantee either with respect to the capital or the return of the portfolio. Due to rounding, numbers presented throughout this document may not add up precisely to the totals provided.

Performance

All performance data for a lump sum, net of fees, include income and assumes reinvestment of income on a NAV to NAV basis. Annualised performances show longer term performance rescaled over a 12 month period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Performance is calculated for the portfolio and individual investor performance may differ as a result thereof. The portfolio is valued at 15h00 daily. Income distributions are net of any applicable taxes. Actual annual figures are available to the investor on request. Prices are published daily and available on the website www.psg.co.za/asset-management and in the daily newspapers. Figures quoted are from Morningstar Inc.

Pricing

Forward pricing is used. Unit trust prices are calculated on a net asset value (NAV) basis, which is the market value of all assets in the Fund including income accruals less permissible deductions divided by the number of units in issue.

Company details

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Conflict of interest disclosure

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Trustees

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We have also witnessed wide divergences in the performances of various global equity markets. The US stock market and economy have continued to perform strongly, with the S&P 500 returning 10.6% for the year to date. In contrast, the MSCI Emerging Markets Index has lost 7.7% and is approaching 20% declines from January highs. The FTSE/JSE All Share Index is down 3.8% year to date, and the FTSE/JSE Shareholder Weighted Index is 8% lower, extending the poor returns of the past four years.

Investor confidence in South Africa matches the gloomy economic backdrop and many domestic assets are trading at or near multi-year lows. Many well-owned stocks on the JSE, including the likes of Steinhoff, MTN, Aspen, Tiger Brands, Mediclinic and Woolworths, have disappointed in recent years and endured aggressive sell-offs. In most cases, starting valuations were high. We continue to avoid stocks that incorporate very high expectations, particularly when we consider how cheaply much of the market trades.

Our perspective
We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. The prevailing fear in local markets has given rise to the opportunity to buy higher-quality stocks (particularly mid-cap industrials) and bonds at wide discounts to what we think they are worth.

Similarly, global stock markets are characterised by very wide divergences in valuations. This bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

Portfolio positioning
The fund retains healthy exposure to cheap domestic stocks. Due to the combination of low levels of earnings and bear market valuations, we expect excellent long-term returns from this component of the portfolio. Specifically, the fund has continued to add to its Old Mutual position after the unbundling of Quilter, partly funded by a selling of Nedbank. We perceive significant positive asymmetry at current share prices – very limited downside and healthy upside.

Rising yields have also seen us add to South African government bond positions. We think that aggressive selling by foreigners has provided the opportunity for equity-like returns from long-dated bonds. It is our view that risk is underwritten by the track record and credibility of the South African Reserve Bank in sustainably anchoring inflation expectations within the target band.

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate direct offshore exposure towards less crowded ideas in recent times. The global stocks the fund owns trade at healthy discounts to our assessments of intrinsic value. 28.7% of the fund is directly invested offshore.

Cash levels remain healthy, with the fund holding 16.8% in cash. This is dry powder that we expect to employ if the opportunities we currently see in many domestic securities become more widespread.

We continue to avoid stocks that we perceive to be overpriced or where we consider risk to be too high. This has served our clients well in recent years: we have avoided many of the disappointing performers on the JSE as they did not meet the high bar we set for portfolio inclusion. While investing offers no guaranteed fail-safe, we believe that our insistence on a margin of safety places the odds in our clients' favour.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity*	47.6%	Domestic equity	47.0%
Domestic cash	16.4%	Domestic cash	16.7%
Domestic gold	0.9%	Domestic gold	0.7%
Domestic bonds	6.2%	Domestic bonds	6.2%
Domestic property	0.8%	Domestic property	0.7%
Foreign cash and gold	0.9%	Foreign cash	0.1%
Foreign equity	22.5%	Foreign equity	25.6%
Foreign property	4.7%	Foreign property	3.0%

**Includes 0.11% effective derivative exposure.*
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by Paul Bosman and Greg Hopkins

Current context

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We have also witnessed wide divergences in the performances of various global equity markets. The US stock market and economy have continued to perform strongly, with the S&P 500 returning 10.6% for the year to date. In contrast, the MSCI Emerging Markets Index has lost 7.7% and is approaching 20% declines from January highs. The FTSE/JSE All Share Index is down 3.8% year to date, and the FTSE/JSE Shareholder Weighted Index is 8% lower, extending the poor returns of the past four years.

Investor confidence in South Africa matches the gloomy economic backdrop and many domestic assets are trading at or near multi-year lows. Many well-owned stocks on the JSE, including the likes of Steinhoff, MTN, Aspen, Tiger Brands, Mediclinic and Woolworths, have disappointed in recent years and endured aggressive sell-offs. In most cases, starting valuations were high. We continue to avoid stocks that incorporate very high expectations, particularly when we consider how cheaply much of the market trades.

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. The prevailing fear in local markets has given rise to the opportunity to buy higher-quality stocks (particularly mid-cap industrials) and bonds at wide discounts to what we think they are worth.

Similarly, global stock markets are characterised by very wide divergences in valuations. This bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

Portfolio positioning

The fund retains healthy exposure to cheap domestic stocks. Due to the combination of low levels of earnings and bear market valuations, we expect excellent long-term returns from this component of the portfolio. Specifically, the fund has continued to add to its Old Mutual position, largely funded by a selling of Nedbank. We perceive significant positive asymmetry at current share prices – very limited downside and healthy upside.

Rising yields have also seen us add to South African government bond positions. We think that aggressive selling by foreigners has provided the opportunity for equity-like returns from long-dated bonds. It is our view that risk is underwritten by the track record and credibility of the South African Reserve Bank in sustainably anchoring inflation expectations within the target band.

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate direct offshore exposure towards less crowded ideas in recent times. The global stocks the fund owns trade at healthy discounts to our assessments of intrinsic value, and at an aggregate price/earnings ratio of 12.1 times. 29% of the fund is directly invested offshore.

Immediate liquidity levels remain healthy, with the fund holding 9.2% in negotiable certificates of deposit and cash. This is dry powder that we expect to employ if the opportunities we currently see in many domestic securities become more widespread.

We continue to avoid stocks that we perceive to be overpriced or where we consider risk to be too high. This has served our clients well in recent years: we have avoided many of the disappointing performers on the JSE, as they did not meet the high bar we set for portfolio inclusion. While investing offers no guaranteed fail-safe, we believe that our insistence on a margin of safety places the odds in our clients' favour.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity	39.5%	Domestic equity	37.9%
Domestic cash and NCDs	8.8%	Domestic cash and NCDs	8.6%
Domestic bonds	24.0%	Domestic bonds	24.8%
Foreign equity	23.4%	Foreign equity	25.3%
Foreign cash	0.8%	Foreign cash	0.5%
Foreign property	3.5%	Foreign property	2.9%

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Regulation 28

The fund is managed according to Regulation 28 of the Pension Funds Act. The South African retirement fund industry is governed by the Pension Funds Act No. 24 of 1956. Regulation 28 of the Pension Funds Act prescribes the maximum limits in asset classes that an approved retirement fund may invest in. Exposures in excess of the limits will be corrected immediately, except where due to a change in the fair value or characteristic of an asset, e.g. market value fluctuations, in which case they will be corrected within a reasonable time period.

Performance

All performance data for a lump sum, net of fees, include income and assumes reinvestment of income on a NAV to NAV basis. Annualised performances show longer term performance rescaled over a 12 month period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Performance is calculated for the portfolio and individual investor performance may differ as a result thereof. The portfolio is valued at 15h00 daily. Income distributions are net of any applicable taxes. Actual annual figures are available to the investor on request. Prices are published daily and available on the website www.psg.co.za/asset-management and in the daily newspapers. Figures quoted are from Morningstar Inc.

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by Paul Bosman and Dirk Jooste

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We have also witnessed wide divergences in the performances of various global equity markets. The US stock market and economy have continued to perform strongly, with the S&P 500 returning 10.6% for the year to date. In contrast, the MSCI Emerging Markets Index has lost 7.7% and is approaching 20% declines from January highs. The FTSE/JSE All Share Index is down 3.8% year to date, and the FTSE/JSE Shareholder Weighted Index is 8% lower, extending the poor returns of the past four years.

Investor confidence in South Africa matches the gloomy economic backdrop and many domestic assets are trading at or near multi-year lows. Many well-owned stocks on the JSE, including the likes of Steinhoff, MTN, Aspen, Tiger Brands, Mediclinic and Woolworths, have disappointed in recent years and endured aggressive sell-offs. In most cases, starting valuations were high. We continue to avoid stocks that incorporate very high expectations, particularly when we consider how cheaply much of the market trades.

Our perspective
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Similarly, global stock markets are characterised by very wide divergences in valuations. This bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

Portfolio positioning
The fund retains healthy exposure to cheap domestic stocks. Due to the combination of low levels of earnings and bear market valuations, we expect excellent long-term returns from this component of the portfolio. Specifically, the fund has continued to add to its Old Mutual position, largely funded by a selling of Nedbank. We perceive significant positive asymmetry at current share prices – very limited downside and healthy upside.

Rising yields have also seen us add to South African government bond positions. We think that aggressive selling by foreigners has provided the opportunity for equity-like returns from long-dated bonds. It is our view that risk is underwritten by the track record and credibility of the South African Reserve Bank in sustainably anchoring inflation expectations within the target band.

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate direct offshore exposure towards less crowded ideas in recent times. The global stocks the fund owns trade at healthy discounts to our assessments of intrinsic value, and at an aggregate price/earnings ratio of 12 times. 17% of the fund is directly invested offshore.

Immediate liquidity levels remain healthy, with the fund holding 22.3% in negotiable certificates of deposit and cash. This is dry powder that we expect to employ if the opportunities we currently see in many domestic securities become more widespread.

We continue to avoid stocks that we perceive to be overpriced or where we consider risk to be too high. This has served our clients well in recent years: we have avoided many of the disappointing performers on the JSE, as they did not meet the high bar we set for portfolio inclusion. While investing offers no guaranteed fail-safe, we believe that our insistence on a margin of safety places the odds in our clients' favour.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity	22.2%	Domestic equity	21.7%
Domestic cash and NCDs	23.9%	Domestic cash and NCDs	21.0%
Domestic bonds	36.8%	Domestic bonds	40.2%
Foreign equity	12.6%	Foreign equity	14.3%
Foreign cash	2.2%	Foreign cash	1.3%
Foreign property	2.3%	Foreign property	1.5%

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Locally, the growth outlook remains weak. This will continue to place pressure on the fiscus, as revenue collection is unlikely to show significant improvement. Furthermore, expectations for shorter-term inflation have risen: in addition to the weaker rand, oil prices have continued to climb (recently resulting in dramatic petrol price increases) and the cost of electricity is also expected to rise over the next four years. This is on the back of the National Energy Regulator's decision to allow Eskom to claw back certain costs, starting with an increase of about 4% by April 2019. The market is now looking to the upcoming medium-term budget policy statement on 24 October 2018, as it is expected to provide key direction on growth initiatives and government's capacity to meet fiscal targets.

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. The prevailing fear in local markets has given rise to the opportunity to buy higher-quality stocks (particularly mid-cap industrials) and bonds at wide discounts to what we think they are worth. Similarly, global stock markets continue to be characterised by very wide divergences in valuations. This bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

In local fixed income markets, interest rates offered by negotiable certificates of deposit (NCDs) are at similar levels to November 2017, when political and fiscal uncertainty was at an all-time high. 12-month NCDs are yielding roughly 8.3% and 60-month NCDs around 9.3%, an attractive real yield given the latest inflation number of 4.9% (August 2018). The market has therefore started to build in expectations of significant interest rate increases, guided by a more hawkish tone from the South Africa Reserve Bank (SARB). (At the SARB's Monetary Policy Committee meeting in September, three members voted to increase the repo rate.) While we believe that the bar for interest rate cuts has risen significantly in the short term, we do not expect the SARB to hike as aggressively as the market has begun to price in. As such, the margin of safety on money market interest rates has increased.

Portfolio positioning

The fund retains healthy exposure to cheap domestic stocks. Due to the combination of low levels of earnings and bear market valuations, we expect excellent long-term returns from this component of the portfolio. Specifically, the fund has continued to add to its Old Mutual position after the unbundling of Quilter, partly funded by a selling of Nedbank. We perceive significant positive asymmetry at current share prices – very limited downside and healthy upside.

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate direct offshore exposure towards less crowded ideas in recent times. The global stocks the fund owns trade at healthy discounts to our assessments of intrinsic value. 5.8% of the fund is directly invested offshore.

Rising yields have also seen us add to South African government bond positions. We think that aggressive selling by foreigners has provided the opportunity for equity-like returns from long-dated bonds. It is our view that risk is underwritten by the track record and credibility of the SARB in sustainably anchoring inflation expectations within the target band. We have also swapped some of our shorter-dated NCDs for longer-dated, higher-yielding counterparts.

Cash levels remain healthy, with the fund holding 43% in cash and NCDs. This is dry powder that we expect to employ if the opportunities we currently see in many domestic securities become more widespread.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity	4.7%	Domestic equity	5.0%
Domestic cash and NCDs	45.7%	Domestic cash and NCDs	43.0%
Domestic bonds	44.3%	Domestic bonds	46.4%
Foreign equity	3.0%	Foreign equity	3.5%
Foreign cash	1.2%	Foreign cash	1.0%
Foreign property	1.1%	Foreign property	1.1%

There may be slight differences in the totals due to rounding.

All data as per Bloomberg to 30 September 2018.

Disclaimer

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Regulation 28

The fund is managed according to Regulation 28 of the Pension Funds Act. The South African retirement fund industry is governed by the Pension Funds Act No. 24 of 1956. Regulation 28 of the Pension Funds Act prescribes the maximum limits in asset classes that an approved retirement fund may invest in. Exposures in excess of the limits will be corrected immediately, except where due to a change in the fair value or characteristic of an asset, e.g. market value fluctuations, in which case they will be corrected within a reasonable time period.

Performance

All performance data for a lump sum, net of fees, include income and assumes reinvestment of income on a NAV to NAV basis. Annualised performances show longer term performance rescaled over a 12 month period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Performance is calculated for the portfolio and individual investor performance may differ as a result thereof. The portfolio is valued at 15h00 daily. Income distributions are net of any applicable taxes. Actual annual figures are available to the investor on request. Prices are published daily and available on the website www.psg.co.za/asset-management and in the daily newspapers. Figures quoted are from Morningstar Inc.

Pricing

Forward pricing is used. Unit trust prices are calculated on a net asset value (NAV) basis, which is the market value of all assets in the Fund including income accruals less permissible deductions divided by the number of units in issue.

Yield

The yield for the portion attributable to fixed income instruments is calculated daily on an annualised basis and is based on the historic yield of the fixed income instruments. The fund returns include returns from property and equity instruments.

Company details

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Conflict of interest disclosure

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Trustee

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Additional information

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PSG Asset Management

PSG Income Fund

Quarterly Portfolio Commentary as at 30 September 2018

by Tyron Green & Greg Hopkins

Current context

Emerging markets have underperformed dramatically in 2018, weighed down by rising US interest rates and turmoil in countries like Turkey and Argentina. This backdrop has seen the rand depreciate to the extent that it is trading weaker than it was before the ANC elective conference in December 2017. Domestic assets have suffered sharp declines this year and many are trading at or near multi-year lows.

Locally, the growth outlook remains weak. This will continue to place pressure on the fiscus, as revenue collection is unlikely to show significant improvement. Furthermore, expectations for shorter-term inflation have risen: in addition to the weaker rand, oil prices have continued to climb (recently resulting in dramatic petrol price increases) and the cost of electricity is also expected to rise over the next four years. This is on the back of the National Energy Regulator's decision to allow Eskom to claw back certain costs, starting with an increase of about 4% by April 2019. The market is now looking to the upcoming medium-term budget policy statement on 24 October, as it is expected to provide key direction on growth initiatives and government's capacity to meet fiscal targets.

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. The prevailing fear in local markets has given rise to the opportunity to buy South African bonds at wide discounts to what we think they are worth.

Interest rates offered by negotiable certificates of deposit (NCDs) are at similar levels to November 2017, when political and fiscal uncertainty was at an all-time high. 12-month NCDs are yielding roughly 8.3% and 60-month NCDs around 9.3%, an attractive real yield given the latest inflation number of 4.9% (August 2018). The market has therefore started to build in expectations of significant interest rate increases, guided by a more hawkish tone from the South Africa Reserve Bank (SARB). (At the SARB's Monetary Policy Committee meeting in September, three members voted to increase the repo rate.) While we believe that the bar for interest rate cuts has risen significantly in the short term, we do not expect the SARB to hike as aggressively as the market has begun to price in. As such, the margin of safety on money market interest rates has increased.

Portfolio positioning

Rising yields have seen us add to South African government bond positions. It is our view that risk is underwritten by the track record and credibility of the SARB in sustainably anchoring inflation expectations within the target band. We have also swapped some of our shorter-dated NCDs for longer-dated, higher-yielding counterparts. In addition, we sold lower-yielding corporate bonds.

Cash levels remain healthy, with the fund holding 64% in cash and NCDs. This is dry powder that we expect to employ if the opportunities we currently see in many domestic securities become more widespread.

Changes in portfolio positioning

Q2 2018			Q2 2018 Restated*	Q3 2018
Fixed-rate notes	67.4%	Domestic bonds	43.3%	35.6%
Floating-rate notes	25.3%	Domestic cash and NCDs	56.7%	64.4%
Domestic cash and NCDs	7.3%			

**Reclassified to align with other fund disclosures.*
There may be slight differences in the totals due to rounding.

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Yield

The yield is calculated daily on an annualised basis. The calculation is based on the historic yield of fixed income instruments.

Performance

All performance data for a lump sum, net of fees, include income and assumes reinvestment of income on a NAV to NAV basis. Annualised performances show longer term performance rescaled over a 12 month period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Performance is calculated for the portfolio and individual investor performance may differ as a result thereof. The portfolio is valued at 15h00 daily. Income distributions are net of any applicable taxes. Actual annual figures are available to the investor on request. Prices are published daily and available on the website www.psg.co.za/asset-management and in the daily newspapers. Figures quoted are from Morningstar Inc.

Pricing

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PSG Asset Management

PSG Money Market Fund

Quarterly Portfolio Commentary as at 30 September 2018

by Lyle Sankar

Current context

Emerging markets have underperformed dramatically in 2018, weighed down by rising US interest rates, a stronger dollar and turmoil in countries like Turkey and Argentina. This backdrop has seen the rand depreciate to the extent that it is trading weaker than it was before the ANC elective conference in December 2017. Domestic assets have suffered sharp declines this year and many are trading at or near multi-year lows.

Locally, the growth outlook remains weak. This will continue to place pressure on the fiscus, as revenue collection is unlikely to show significant improvement. Furthermore, expectations for shorter-term inflation have risen: in addition to the weaker rand, oil prices have continued to climb (recently resulting in dramatic petrol price increases) and the cost of electricity is also expected to rise over the next four years. This is on the back of the National Energy Regulator's decision to allow Eskom to claw back certain costs, starting with an increase of about 4% by April 2019. The market is now looking to the upcoming medium-term budget policy statement on 24 October, as it is expected to provide direction on growth initiatives and government's capacity to meet fiscal targets.

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. The prevailing fear in local markets and higher near-term inflationary pressures have provided an opportunity to buy money market instruments at attractive yields.

Interestingly, short-term interest rates are at similar levels to November 2017, when political and fiscal uncertainty was at an all-time high. 12-month negotiable certificates of deposit are yielding roughly 8.3%, an attractive real yield given the latest inflation number of 4.9% (August 2018). The market has therefore started to build in expectations of significant interest rate increases, guided by a more hawkish tone from the South Africa Reserve Bank (SARB). (At the SARB's Monetary Policy Committee meeting in September, three members voted to increase the repo rate.) While we believe that the bar for interest rate cuts has risen significantly in the short term, we do not expect the SARB to hike as aggressively as the market has begun to price in. As such, the margin of safety on money market interest rates has increased.

Portfolio positioning

The fund's maturity profile has been extended as yields on the longer end of the cash curve have increased. We have also added significantly to the fund's exposure to RSA National Treasury bills, thereby increasing its overall liquidity. We are currently close to full duration.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Linked NCDs/ Floating-rate notes	20.0%	Linked NCDs/Floating-rate notes	21.4%
Step rate notes	11.7%	Step rate notes	11.9%
NCDs	55.7%	NCDs	41.0%
Treasury bills	6.9%	Treasury bills	24.0%
Call deposits	3.0%	Call deposits	0%
Corporate bonds	2.7%	Corporate bonds	1.7%

There may be slight differences in the totals due to rounding.

All data as per Bloomberg to 30 September 2018.

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Money Market

The PSG Money Market Fund maintains a constant price and is targeted at a constant value. The quoted yield is calculated by annualizing the average 7 day yield. A money market portfolio is not a bank deposit account. Excessive withdrawals from the portfolio may place the portfolio under liquidity pressures and in such circumstances a process of ring-fencing of withdrawal instructions and managed payouts over time may be followed. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument. In most cases the return will merely have the effect of increasing or decreasing the daily yield but in the case of abnormal losses it can have the effect of reducing the capital value of the portfolio. Due to rounding, numbers presented throughout this document may not add up precisely to the totals provided.

Regulation 28

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Performance

All performance data for a lump sum, net of fees, include income and assumes reinvestment of income on a NAV to NAV basis. Annualised performances show longer term performance rescaled over a 12 month period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Performance is calculated for the portfolio and individual investor performance may differ as a result thereof. The portfolio is valued at 15h00 daily. Income distributions are net of any applicable taxes. Actual annual figures are available to the investor on request. Prices are published daily and available on the website www.psg.co.za/asset-management and in the daily newspapers. Figures quoted are from Morningstar Inc.

Pricing

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Trustees

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Additional information

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Current context

Emerging markets have underperformed dramatically in 2018, weighed down by rising US interest rates and turmoil in countries like Turkey and Argentina. We have also witnessed wide divergences in the performances of various global equity markets. The US stock market and economy have continued to perform strongly, with the S&P 500 returning 10.6% for the year to date. In contrast, the MSCI Emerging Markets Index has lost 7.7% and is approaching 20% declines from January highs.

The US remains the standout performer when taking a longer-term view. Despite the often-cited nine-year (and counting) global bull market, many major markets are still below pre-global financial crisis (GFC) highs when measured in US dollars. While the picture looks a bit better when accounting for dividends, the US market has strongly outpaced all others over the period since pre-crisis highs (see Table 1).

Table 1: Selective market performances* since the GFC

	% Total return from GFC low (in USD incl. dividends)	% return from pre-GFC high (in USD)	% Total return from pre-GFC high (in USD incl. dividends)
S&P 500	420%	87%	136%
MSCI World	310%	34%	80%
Australia AS30	293%	-18%	50%
JSE All-share	218%	-16%	17%
MSCI Emerging Markets	203%	-22%	6%
FTSE 100 (UK)	187%	-28%	9%
CAC 40 (France)	184%	-24%	13%
Topix (Japan)	176%	2%	30%
Shanghai Composite	99%	-49%	-35%

**Returns in USD, not annualised, for each individual market GFC low and pre-GFC high to 28 September 2018.*
Sources: PSG Asset Management; Bloomberg

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. While a favourable economic backdrop in the US and good earnings growth support current high valuations, we are not willing to own securities when expected long-term returns will likely be low (at best) and the risk of capital loss is high. Fortunately, global stock markets continue to be characterised by very wide divergences in valuations, which bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

Portfolio positioning

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate exposure towards less crowded ideas over the past year (as we have written about in previous commentaries). Over the most recent quarter, the fund sold its remaining shareholding in Berkshire Hathaway. When we invested in the company many years ago, it was trading at a significant discount to its cheap underlying holdings. In our view, this is no longer the case. While Berkshire Hathaway remains a great company, it therefore no longer satisfies our requirement for a wide margin of safety. We also exited Imperial Brands, Qualcomm and Nordstrom after their share prices rallied strongly and exceeded our estimates of intrinsic value.

We have previously written about the opportunity in Japanese financial companies and added to the fund's positions over the past quarter. Collectively, Japanese financials accounted for 9.5% of the fund, compared to 6.9% in June. The fund also added to its positions in Babcock International, Transocean, Old Mutual, L Brands and Glencore during bouts of share price weakness.

From a regional perspective, 39% of the fund was invested in US-listed equities as at quarter end. This may appear high, given the extended valuations in that market. However, it should be noted that only 11.5% of the fund's holdings have direct exposure to the US economy. Holdings are also in areas that are currently unpopular and uncrowded, such as real estate and retail.

The fund's equity holdings are of similar quality but significantly cheaper than the average company in the market. Additionally, these holdings are trading at cheap valuations relative to their own histories, and on below-normal earnings levels. This gives us cause for optimism that the fund is well positioned to deal with the uncertain environment investors currently face.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity	4.3%	Domestic equity	4.5%
Domestic cash	0.2%	Domestic cash	0.3%
Foreign equity	84.4%	Foreign equity	76.2%
Foreign property	1.8%	Foreign property	7.2%
Foreign cash	9.3%	Foreign cash	11.8%

Q2 2018		Q3 2018	
US	43.5%	US	39.1%
Europe	5.8%	Europe	6.0%
UK	14.1%	UK	12.6%
Asia ex Japan	6.3%	Asia ex Japan	6.1%
Japan	6.9%	Japan	9.5%
Canada	9.0%	Canada	9.7%
Africa	4.3%	Africa	4.5%
Other	0.6%	Other	0.4%
Cash	9.5%	Cash	12.1%

There may be slight differences in the totals due to rounding.

Please note that this commentary is for the US dollar-denominated PSG Global Equity Sub-Fund. The PSG Global Equity Feeder Fund is 100% invested in the underlying US dollar fund. However, there may small short-term valuation, trading and translation differences between the two funds.

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Feeder Funds

A Feeder Fund is a portfolio which, apart from assets in liquid form, invests in a single portfolio of a collective investment scheme, which levies its own charges and which could result in a higher fee structure for the feeder fund.

Performance

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Additional information

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by Philipp Wörz and Greg Hopkins

Current context

Emerging markets have underperformed dramatically in 2018, weighed down by rising US interest rates and turmoil in countries like Turkey and Argentina. We have also witnessed wide divergences in the performances of various global equity markets. The US stock market and economy have continued to perform strongly, with the S&P 500 returning 10.6% for the year to date. In contrast, the MSCI Emerging Markets Index has lost 7.7% and is approaching 20% declines from January highs.

The US remains the standout performer when taking a longer-term view. Despite the often-cited nine-year (and counting) global bull market, many major markets are still below pre-global financial crisis (GFC) highs when measured in US dollars. While the picture looks a bit better when accounting for dividends, the US market has strongly outpaced all others over the period since pre-crisis highs (see Table 1).

Table 1: Selective market performances* since the GFC

	% Total return from GFC low (in USD incl. dividends)	% return from pre-GFC high (in USD)	% Total return from pre-GFC high (in USD incl. dividends)
S&P 500	420%	87%	136%
MSCI World	310%	34%	80%
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Topix (Japan)	176%	2%	30%
Shanghai Composite	99%	-49%	-35%

**Returns in USD, not annualised, for each individual market GFC low and pre-GFC high to 28 September 2018.*
Sources: PSG Asset Management; Bloomberg

Our perspective

We apply a repeatable investment process, according to which we allocate capital to securities we consider undervalued and take profits where prices are high. While a favourable economic backdrop in the US and good earnings growth support current high valuations, we are not willing to own securities when expected long-term returns will likely be low (at best) and the risk of capital loss is high. Fortunately, global stock markets continue to be characterised by very wide divergences in valuations, which bodes well for returns for investors who are prepared to invest in uncrowded stocks and take a long-term view.

Portfolio positioning

Elevated valuations and high levels of profits of popular global stocks – particularly in the US – have seen us reallocate exposure towards less crowded ideas over the past year (as we have written about in previous commentaries). Over the most recent quarter, the fund sold its remaining shareholding in Berkshire Hathaway. When we invested in the company many years ago, it was trading at a significant discount to its cheap underlying holdings. In our view, this is no longer the case. While Berkshire Hathaway remains a great company, it therefore no longer satisfies our requirement for a wide margin of safety. We also exited Imperial Brands, Qualcomm and Nordstrom after their share prices rallied strongly and exceeded our estimates of intrinsic value.

We have previously written about the opportunity in Japanese financial companies and added to the fund's positions over the past quarter. Collectively, Japanese financials accounted for 7.7%) of the fund, compared to 5.4% in June. The fund also added to its positions in Babcock International, Transocean, Old Mutual, L Brands and Glencore during bouts of share price weakness.

From a regional perspective, 32% of the fund was invested in US-listed equities as at quarter end. This may appear high, given the extended valuations in that market. However, it should be noted that only 10% of the fund's holdings have direct exposure to the US economy. Holdings are also in areas that are currently unpopular and uncrowded, such as real estate and retail.

The fund's equity holdings are of similar quality but significantly cheaper than the average company in the market. Additionally, these holdings are trading at cheap valuations relative to their own histories, and on below-normal earnings levels. This gives us cause for optimism that the fund is well positioned to deal with the uncertain environment investors currently face.

Cash levels remain healthy, with the fund holding 27.8% in cash. This is dry powder that we expect to employ if the opportunities we currently see in uncrowded securities become more widespread.

Changes in portfolio positioning

Q2 2018		Q3 2018	
Domestic equity	3.3%	Domestic equity	3.5%
Domestic cash	0.6%	Domestic cash	0.8%
Foreign equity	61.0%	Foreign equity	62.1%
Foreign property	8.0%	Foreign property	6.5%
Foreign gold	1.7%	Foreign gold	1.2%
Foreign cash	25.5%	Foreign cash	25.9%

Q2 2018		Q3 2018	
US	34.3%	US	32.0%
Europe	4.6%	Europe	4.8%
UK	11.9%	UK	10.6%
Asia ex Japan	5.2%	Asia ex Japan	5.0%
Japan	5.4%	Japan	7.7%
Canada	7.5%	Canada	8.1%
Africa	3.3%	Africa	3.5%
Other	0.5%	Other	0.4%
Cash	27.3%	Cash	27.9%

There may be slight differences in the totals due to rounding.

Please note that this commentary is for the US dollar-denominated PSG Global Flexible Sub-Fund. The PSG Global Flexible Feeder Fund is 100% invested in the underlying US dollar fund. However, there may small short-term valuation, trading and translation differences between the two funds.

All data as per Bloomberg to 30 September 2018.

Disclaimer

Collective Investment Schemes in Securities (CIS) are generally medium to long-term investments. The value of participatory interests (units) or the investment may go down as well as up and past performance is not a guide to future performance. Fluctuations or movements in the exchange rates may cause the value of underlying international investments to go up or down. CIS are traded at ruling prices and can engage in borrowing and scrip lending. The Fund may borrow up to 10% of its market value to bridge insufficient liquidity. Where foreign securities are included in a portfolio, the portfolio is exposed to risks such as potential constraints on liquidity and the repatriation of funds, macroeconomic, political, foreign exchange, tax, settlement and potential limitations on the availability of market information. The portfolios may be capped at any time in order for them to be managed in accordance with their mandate. Excessive withdrawals from the portfolio may place the portfolio under liquidity pressures and in such circumstances a process of ring-fencing of withdrawal instructions and managed payouts over time may be followed. PSG Collective Investments (RF) Limited does not provide any guarantee either with respect to the capital or the return of the portfolio. Due to rounding, numbers presented throughout this document may not add up precisely to the totals provided.

Feeder Funds

A Feeder Fund is a portfolio which, apart from assets in liquid form, invests in a single portfolio of a collective investment scheme, which levies its own charges and which could result in a higher fee structure for the feeder fund.

Performance

All performance data for a lump sum, net of fees, include income and assumes reinvestment of income on a NAV to NAV basis. Annualised performances show longer term performance rescaled over a 12 month period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Performance is calculated for the portfolio and individual investor performance may differ as a result thereof. The portfolio is valued at 15h00 daily. Income distributions are net of any applicable taxes. Actual annual figures are available to the investor on request. Prices are published daily and available on the website www.psg.co.za/asset-management and in the daily newspapers. Figures quoted are from Morningstar Inc.

Pricing

Forward pricing is used. Unit trust prices are calculated on a net asset value (NAV) basis, which is the market value of all assets in the Fund including income accruals less permissible deductions divided by the number of units in issue.

Company details

PSG Collective Investments (RF) Limited is registered as a CIS Manager with the Financial Sector Conduct Authority, and a member of the Association of Savings and Investments South Africa (ASISA) through its holdings company PSG Konsult Limited. The management of the portfolio is delegated to PSG Asset Management (Pty) Ltd, an authorised Financial Services Provider under the Financial Advisory and Intermediary Services Act 2002, FSP no 29524. PSG Asset Management (Pty) Ltd and PSG Collective Investments (RF) Limited are subsidiaries of PSG Konsult Limited. PSG Collective Investments (RF) Limited can be contacted on +27(21) 799 8000; (toll free) 0800 600 168, via email assetmanagement@psg.co.za.

Conflict of interest disclosure

The Fund may from time to time invest in a portolio managed by a related party. PSG Collective Investments (RF) Limited or the fund manager may negotiate a discount in fees charged by the underlying portfolio. All discounts negotiated are reinvested in the Fund for the benefit of the investors. Neither PSG Collective Investments (RF) Limited nor PSG Asset Management (Pty) Ltd retains any portion of such discount for their own accounts. The fund manager may use the brokerage services of a related party, PSG Securities Ltd.

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Additional information

Additional information is available free of charge on the website www.psg.co.za/asset-management and may include publications, brochures, forms and annual reports.