PSG Asset Management

ANGLES & PERSPECTIVES

THIRD QUARTER 2014

CONTENTS

INTRODUCTION

By Anet Ahern

Anet has over 25 years' experience in investment and business management. After starting her career at Allan Gray in 1986, where she fulfilled various roles in trading and investment management, she worked as a portfolio manager at Syfrets, and later BoE Asset Management, where she was CIO and CEO. She also spent six years at Sanlam, where she was the CEO of Sanlam Multi Manager International, with assets totalling R100 billion in local and global mandates. Anet joined PSG Asset Management as CEO in 2013.

We are proud of the milestones we reached in 2014

Another eventful year in the investment markets is drawing to a close. For PSG Asset Management, it was a year of milestones. Our funds under management surpassed R20 billion and our Manco assets R50 billion. We climbed up to second place in the Plexcrown rankings and one of our flagship funds, the PSG Flexible Fund, celebrated its tenth anniversary with more than R5 billion in assets. Five of our funds are now larger than R1 billion in size.

Despite our achievements, our priority remains to protect and grow our investors' money

As much as we are proud of these achievements, we remain mindful of the fact that we are trusted to look after our investors' money as if it were our own, in an environment that has certainly thrown a few curve balls at investment managers. Most notable were the failure of African Bank and a renewed focus on the risk inherent to investing in credit markets. If you combine that with a weakening currency, crippling strikes and volatile global equity markets, it's understandable that investors may be somewhat apprehensive at the moment.

Risk remains a key consideration in our investment decisions

In our portfolio positioning, we have always prioritised risk in our assessment of every investment opportunity. This has sometimes led to our positioning being somewhat ahead of the risks that we try to mitigate playing out. Examples of this in 2014 include a higher weighting in cash in all our portfolios, a full offshore weighting, a very strict credit process that enabled us to avoid what we perceived as asymmetrical risk-reward situations, and a notable absence of widely held South African listed shares that we believed were overpriced.

In this edition, we explain and illustrate different factors that determine how we invest

It is not enough just to avoid risk. To make our clients' investments really work for them, we also need to take a longer-term view. We must constantly sharpen our pencils so that we can be brave when others are fearful and take advantage of the opportunities that short-termism inevitably brings. In this edition, Lisa Haakman explains how we saw an opportunity in Capitec when many investors were blinded by contagion.

It is also not enough to just invest in apparently cheap opportunities, as Greg Hopkins, our CIO, highlights when he warns of the pitfalls of value investing and how we aim to avoid them. Paul Bosman, manager of the PSG Balanced Fund and co-manager of the PSG Stable Fund, talks about what investors can expect from our multi-asset funds by discussing the difference between expecting and predicting. This is key to the way we view investments.

In the Fund Focus article, Shaun le Roux, manager of our 5-Plexcrown PSG Equity Fund talks about the Fund positioning and his 12 years as manager of the Fund.

We wish you all the best for year-end

We trust that you will enjoy reading about our thinking and our approach. We hope it encourages you that a consistent, long-term application of a philosophy that has been proven successful, is your best ally during these turbulent times. We wish you a restful break over year-end and thank you for your support and interest.

ANTIDOTES TO THE PITFALLS OF VALUE INVESTING

By Greg Hopkins

Greg is a CA (SA) and a CFA Charterholder. He is PSG Asset Management's Chief Investment Officer.

Many articles have been written recently about the pitfalls of value investing. This is perhaps a result of the relative underperformance of many traditional South African value managers over the past five years (see Graph 1 on the next page).

Some of these well-reasoned arguments for the relative underperformance by value managers are as follows[1]:

1. Most institutional asset managers in South Africa are value-biased, making this segment overcrowded and rendering outperformance difficult.
2. Value investors ignore the fact that certain industries they invest in are in structural decline, and therefore introduce the risk of investing in value traps.
3. Value investors take large off-benchmark bets, which introduce significant business risk.

At the outset we need to point out that we at PSG Asset Management are value investors in the sense that we are consistently looking for undervalued opportunities. However, we believe that there are important factors that we incorporate into our process that will ensure that we avoid the pitfalls mentioned above.

1. Most institutional asset managers in South Africa are value-biased, making this segment overcrowded and rendering outperformance difficult

We would agree that the South African investing landscape is competitive – we have a group of highly qualified peers with a universe of opportunities that is potentially limited by the existence of exchange controls. However, we believe that long-term outperformance for the value-biased manager is very possible.

Given the competitive nature of our industry and the efficiency with which it has reduced potential alpha-creating opportunities, we believe it is imperative to have the largest possible universe to invest in. Being able to invest in mid cap opportunities and offshore, as we do at PSG Asset Management, would therefore significantly reduce competition. In fact, we would argue that, given the size of the largest managers in the industry, the competitive environment is now less competitive than it has been for years.

Analogous to this, we believe that it also important not to pigeonhole oneself into a specific style box, which further restricts one's universe, for example being a value or growth manager. Being only a 'deep value' or 'quality' or 'growth' manager, lends to what Charlie Munger calls the 'man with a hammer syndrome'. For the man with a hammer, each problem or idea looks like a nail. 'Deep value' managers who only 'buy cheap' have arguably fallen into this trap over the past few years.

We at PSG Asset Management like to look at quality and value factors in the same investment and try always to stay open minded while investing in all segments of the market.

We discuss our approach to making investment decisions in more detail in the Fund Focus article about the PSG Equity Fund on page 16.

1 'Value Investing is not dead', Lambrides, BDLive, November 2013

Graph 1: ASISA general equity – percentile ranking of 'deep value' fund composite

* Composite index of the rolling three-year perfomance of a number of funds that are believed to follow a 'deep value' philosophy. The lower the percentile ranking, the better the performance of the composite relative to the general equity sector.

Sources: Morningstar, PSG Asset Management

2. Value investors ignore the fact that certain industries they invest in are in structural decline, and therefore have a high risk of investing in value traps

A significant source of underperformance for managers comes from buying 'value traps'. These are companies that are perceived to be cheap initially, but prove to be otherwise over the long term. Structural challenges in an industry can result in deteriorating returns on capital for industry players as well as the prevention of mean reversion, that is, a return to previous mean returns.

Warren Buffett has a great analogy when he refers to value traps as frogs that stay frogs and don't turn into princes when kissed.

We believe that it is important to have a quality overlay in one's investment process – an important antidote to buying value traps. Buying businesses with a competitive advantage and that have management teams with a proven track record are two parts of the three-part checklist that we use for all our equity and credit investments.

In fact, not making large mistakes and avoiding value traps over time often contributes more to long-term sustainable outperformance than hitting a few big winners out of the park.

Examples of value traps over the past few years are South Africa's deep level single commodity industries such as gold and platinum, as well as African Bank. The former have inflexible cost bases and falling ore grades, while the latter has a potentially broken business model.

We at PSG Asset Management have made numerous mistakes over the years. However, our long-term track record shows that starting with quality in mind and buying quality when it is out of favour will ultimately get the odds of success in our favour.

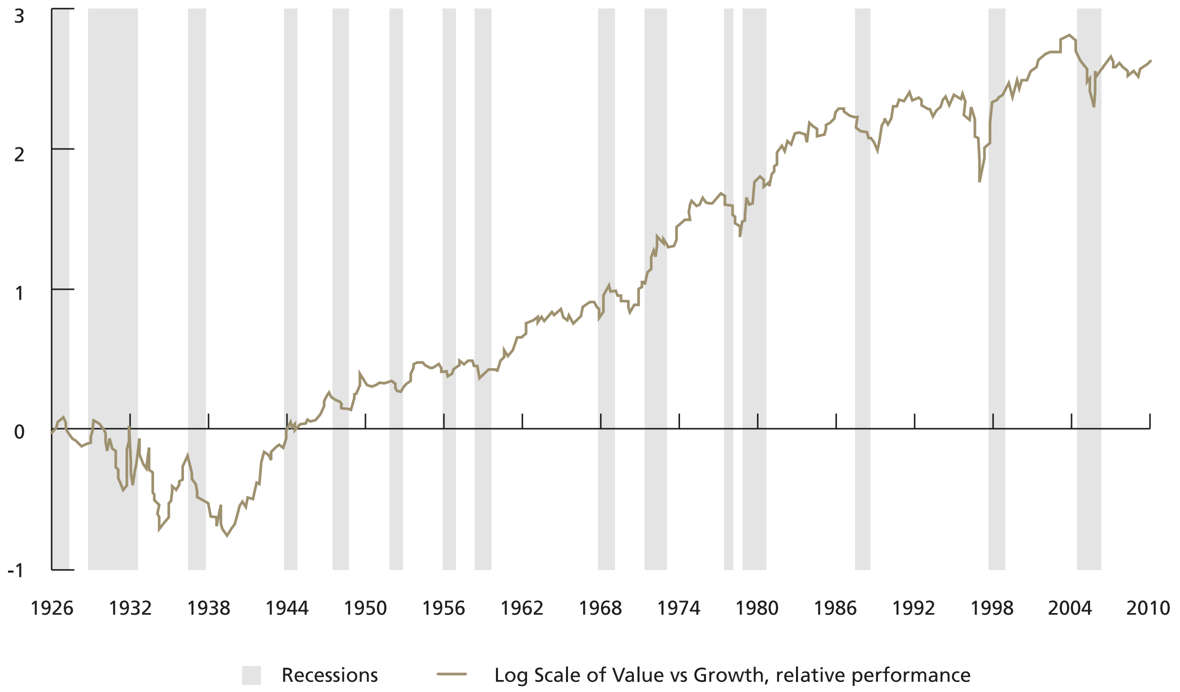
3. Value investors take large off-benchmark bets, which introduces significant business risk

We would disagree. Being benchmark conscious – that is, buying shares only because they are in the benchmark – leads smart investors to buy overvalued shares for the fear of short-term underperformance. This situation is exacerbated by the current potential overvaluation of many of the largest companies in the benchmark (the JSE Indi 25 has only been this expensive in aggregate three times over the past 50 years).

Unconstrained investors like ourselves have a responsibility to ensure that the investors in our funds understand our philosophy, process and the longer-term time frame that we use when evaluating investment opportunities. We also have the responsibility to ensure that we continue to diversify our investor base.

We believe that to be unconstrained one needs to have the largest possible universe to invest in, a strong focus on quality to avoid value traps, and a ruthless eye on margin of safety to avoid permanent loss of capital. If we can do this consistently and with an open mind, owning companies in our funds that others don't becomes a significant attribute.

Graph 2: Relative performance of value versus growth in the US



Monthly data: Average returns of Fama-French large/small growth and large/small value benchmark portfolios

Sources: Bank of America Merrill Lynch Global Investment Strategy, Fama-French

4. Is value investing an out-of-favour segment of the market that provides opportunities?

Given the recent underperformance of the deeper value fund management composite discussed above, and the capitulation of investors from this space, we are naturally attracted to any potential opportunities that might arise in the universe of companies that these managers mine. Inflection points often occur at maximum points of pessimism after investors have extrapolated the recent past in perpetuity. Many of the recent arguments against value investing are arguably just a symptom of this extrapolation.

Indeed, the value style has outperformed in the US in three out of five years (60% of the time) since 1926 (see Graph 2). The style does however tend to underperform in periods of recession and below-trend growth, which has characterised the world since the great financial crisis. Any pick-up in global growth could see a resumption in a mean reversion of margins and earnings in companies that investors have long given up on.

WHAT TO EXPECT FROM YOUR INVESTMENT IN OUR MULTI-ASSET FUNDS

By Paul Bosman

Paul joined PSG in 2004 when he began working for PSG Capital as an equity analyst. In November 2004 he joined the PSG Tanzanite team as an equity analyst. With the incorporation of PSG Tanzanite into PSG Asset Management, Paul continued as an equity analyst, specialising in both local and offshore listed companies. In 2011, Paul became a Portfolio Manager at PSG Asset Management and is responsible for the management of the PSG Balanced Fund and PSG Stable Fund.

In this article, we explore the underlying currents that will inevitably influence the short- and medium-term performance of our multi-asset funds.

When you predict something, you focus on the details. When you have an expectation, you look at all the driving factors and derive a likely outcome based on these factors.

For example, you cannot predict exactly what time your teenage son will be home, but you certainly have an expectation. Your expectation would be a function of a number of factors, including his track record of arriving home within curfew and the nature of the outing – a braai tends to be harder to leave than a school play.

Real yields affect our expectations for the markets

We cannot offer our clients predictions of what the markets will deliver but we certainly are able to share our expectations. When we refer to 'the markets' we refer to all investable assets in the universe of our respective funds. To be specific, it would include cash on call, longer-term deposits, short-term bonds, long-term bonds, inflation-linked bonds, listed property and equities.

Our expectations are naturally a function of a number of factors. One of these factors is that, over time, assets offer a real yield (yield in excess of inflation) that is proportionate to their risk. When the real yield is too low, we become careful.

What drives real yield levels?

There is a finite amount of investable assets in the markets at any given time and money flows between these assets. If market participants are chasing a specific asset class, the price of the asset class would go up and the yield down. If, for example, nobody wants to own bonds and everybody wants to own equities, the yields on bonds will go up and the yields on equities will go down. Even though this is an extreme case, it is relevant for this article because we are currently operating in an extreme environment.

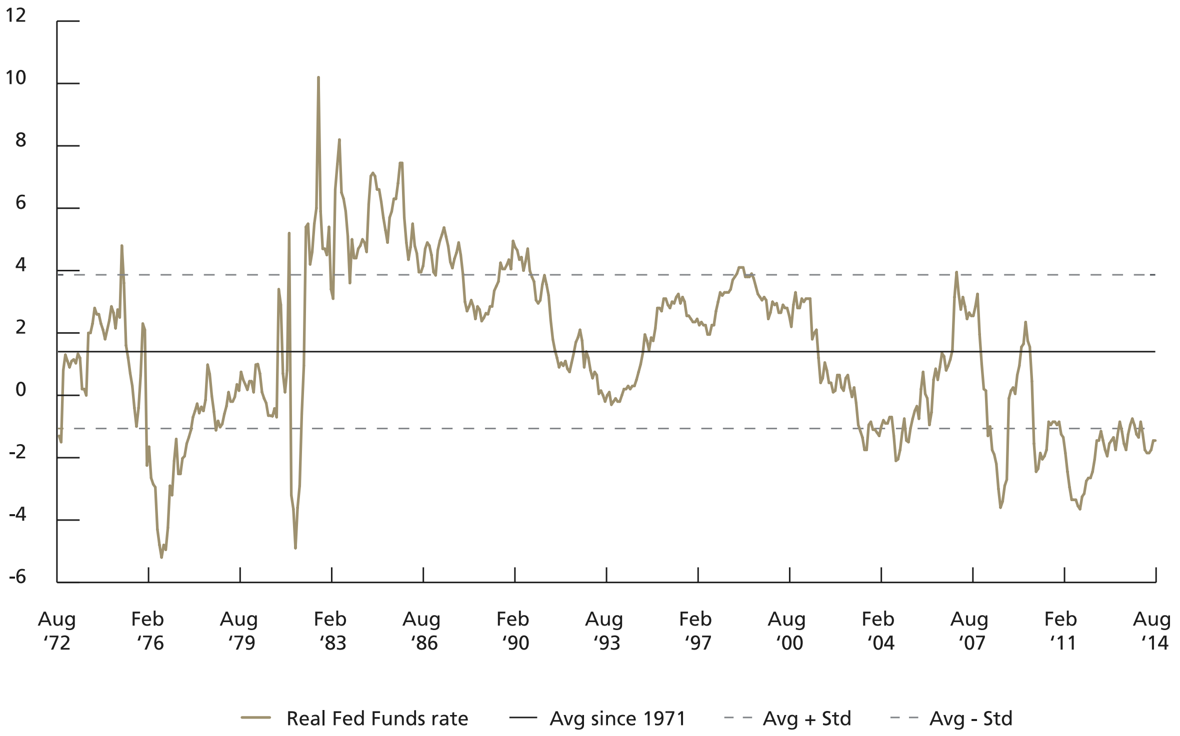
Cash is currently offering a negative real yield, but what are the alternatives?

Graphs 1 and 2 on the next page show the real yield offered by cash over time. Cash is generally categorised as money market instruments of shorter than one year. We are using the rate as set by the central banks as a proxy for the cash yield.

In both the US and South Africa, cash is currently offering a negative real yield, in other words one loses buying power over time by investing in cash. For obvious reasons, cash is currently a rather unpopular investment and investors are gravitating towards other asset classes. Which asset classes would be the most affected by this? Government bonds would be the best substitute for cash because these instruments also offer a predictable yield. Graphs 3 and 4 on page 7 clearly show that yields on government bonds have in fact contracted significantly as investors are moving their money from cash to bonds.

If you intended making use of government bonds to achieve your required return, the current environment would pose a problem, as the yields would most probably be too low. As a result, you would need to move up the risk spectrum and most probably invest in corporate bonds. Graph 5 on page 8 shows how the yields on corporate bonds in the US have declined over the last number of years as money has rushed into these instruments.

Graph 1: The real yields of cash in the US (January 1971 to September 2014)

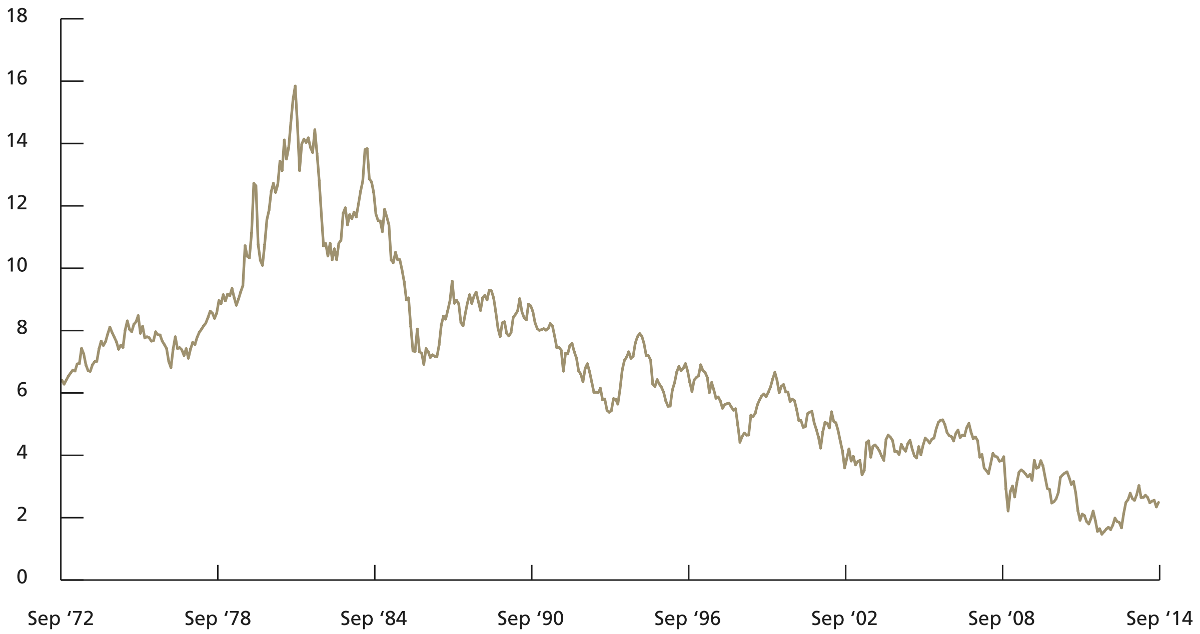


Source: Bloomberg

Graph 2: The real yields of cash in South Africa (March 1998 to September 2014)

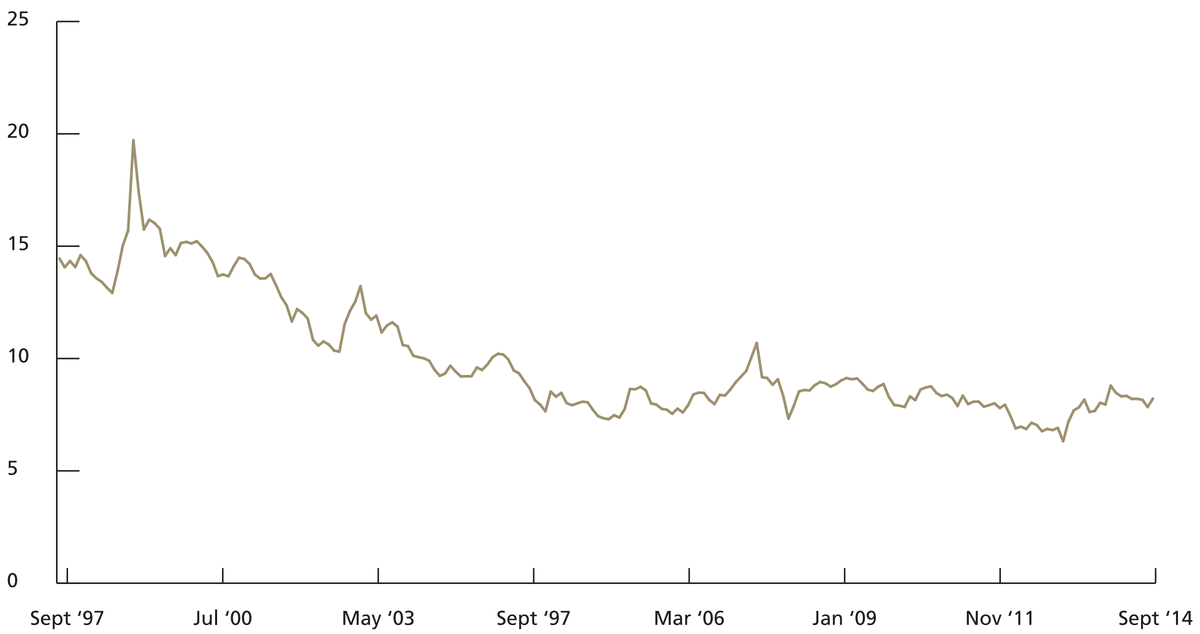
Source: Bloomberg

Graph 3: US 10-year government bonds yields (January 1971 to September 2014)



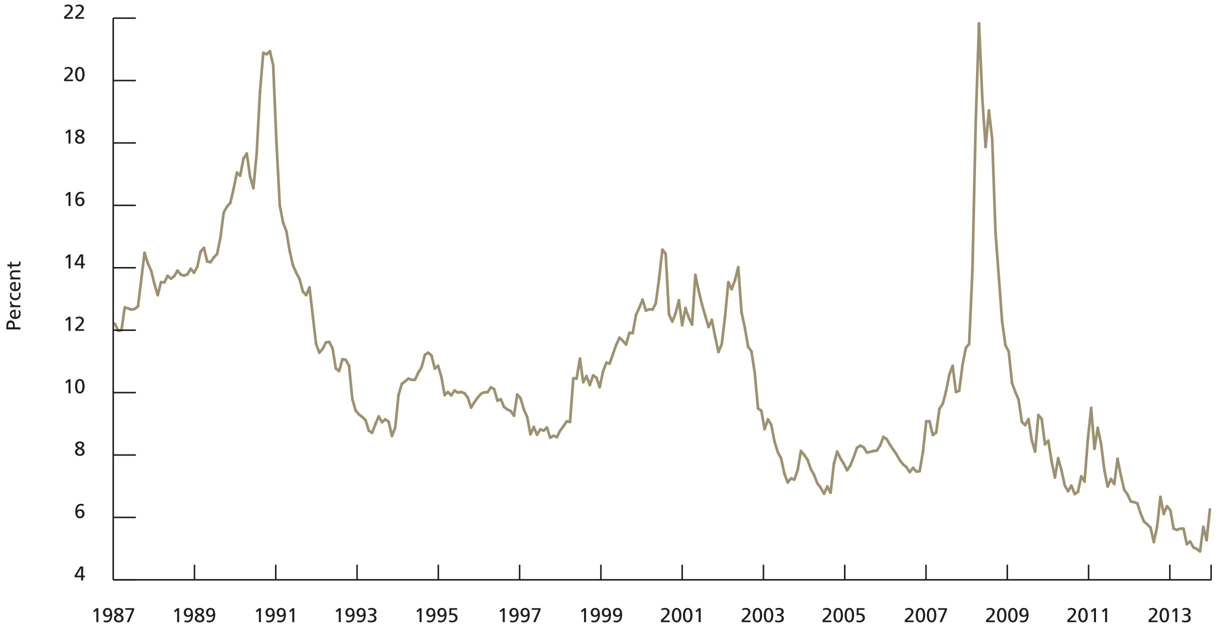
Source: Bloomberg

Graph 4: South African 10-year government bonds yields (June 1997 to September 2014)



Source: Bloomberg

Graph 5: Barclays US Corporate High Yield Index (January 1987 to September 2014)



Source: Bloomberg

However, corporate bonds may also not offer a sufficient yield for many investors and they would be compelled to move even further up the risk spectrum to property or high quality equities with reasonably predictable dividend streams. Graphs 6 and 7 on the next page show how the dividend yields on listed properties as well as stable dividend payers have declined.

It is inevitable that the real yield on cash is restored, but when does the trend start to reverse?

Chart 1 on page 10 is a visual presentation of everything that we've discussed so far.

When will cash flow back down the risk spectrum and asset prices start to deflate? We think it is when the real yield on cash is restored. This is inevitable – in the long run, cash should have a positive real yield, otherwise a country's economy could experience all kinds of problems, including currency devaluation, high inflation and a disincentive to save. The long-run average real yields offered on cash in the US and South Africa as shown in Graphs 1 and 2 confirm this.

We believe investing in cash now will offer opportunities later

Firstly, we are disciplined in our philosophy to only invest when real yields make sense in proportion to the accompanying risk. There are many securities that we currently regard as too expensive and, as a result we hold cash – despite the negative real yield. Why are we prepared to break rule number one - being wary of low yields - when it comes to cash?

The answer is that when interest rates normalise, there could be plenty of opportunities for contrarian investors like ourselves who were prepared to take a little bit of pain in the short term to have cash available when security prices offer value again. Also, cash will not experience a drawdown as yields normalise, so the risk seems tolerable.

We focus on what we do know to determine our positioning in the current environment. We don't know when cash rates will rise, but we do know the following:

- Assets prices are unlikely to move such that yields are significantly lower than current levels for any significant period of time.
- When asset prices do normalise, there could be very good buying opportunities for those who have cash.

Instead of trying to get our timing exactly right (which is the part we cannot predict) we have rather positioned our portfolios in line with what we do know.

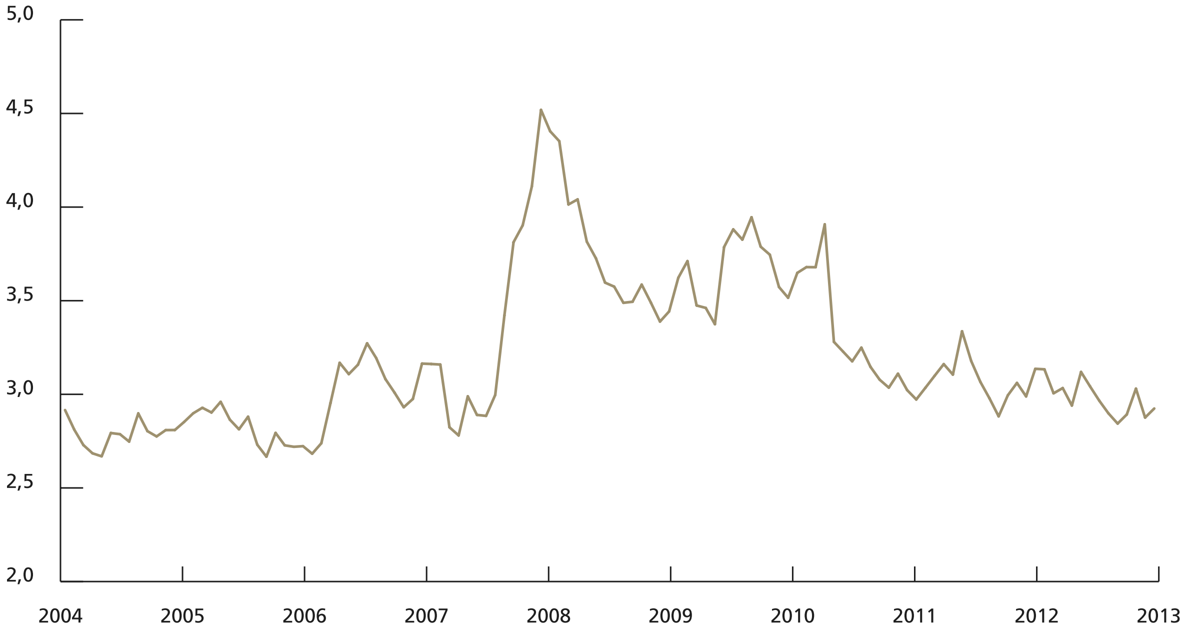
We do not hold government bonds

The current real yields offered by nominal bonds are generally not sufficient to reward for the accompanying risk. For example, in the US, real yields on 10-year government bonds are 0.8%, which is significantly below the 20-year average of 2.0%. In South Africa, the current real yield of 1.9% on 10-year government bonds is still approximately 2% below their long-term average.

Graph 6: Dividend yield of the FTSE/JSE Listed Property Index (May 2005 to September 2014)

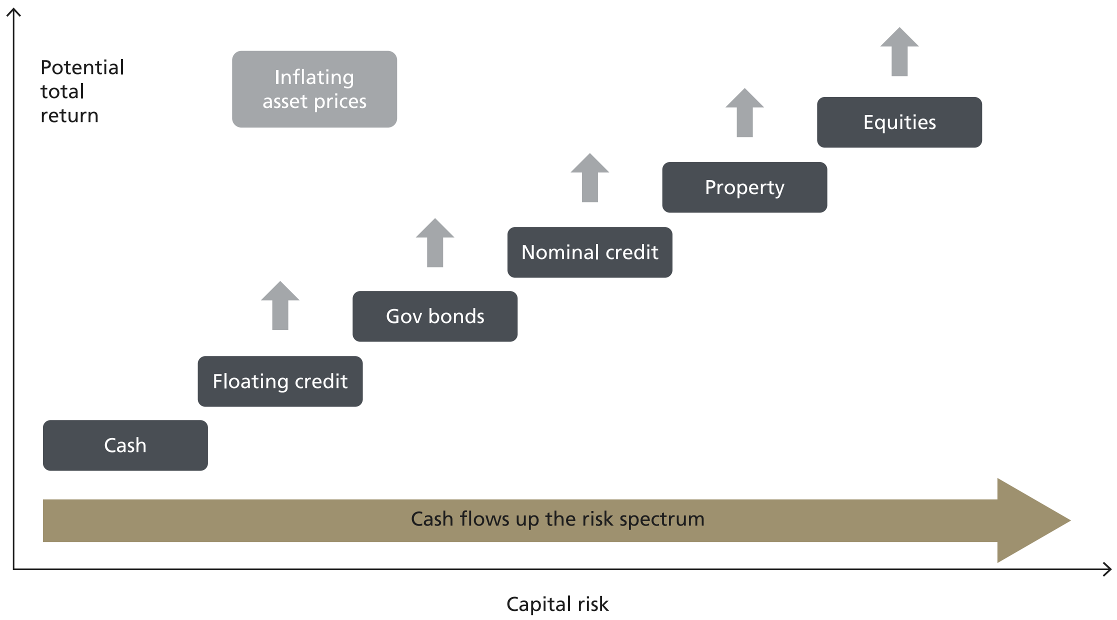
Source: Bloomberg

Graph 7: Dividend yield of the S&P500 Food, Beverage and Tobacco Index (October 2004 to September 2014)



Source: Bloomberg

Chart 1: The inflating effect on all asset classes



Source: PSG Asset Management

Bonds will eventually have to re-price to offer higher real yields. We therefore do not hold any government bonds.

We only hold selected domestic corporate bonds

Graph 5 shows that it is hard to find corporate bonds that offer attractive real yields. In South Africa, there are a few exceptions, especially after the failure of African Bank. We therefore do hold selected domestic corporate bonds. These bonds have all been through a very rigorous in-house credit analysis and we are confident that we will earn attractive real yields from them over time.

We do not hold listed property

Listed property (referring to the FTSE/JSE Listed Property Index) currently offers a zero real yield and, unlike the case of corporate bonds, we have not been able to find any individual opportunities in this asset class.

Stable dividend payers are expensive

The hunt for yield has attracted money to the stable dividend payers in particular. As a result, our bottom-up process has found very limited opportunities in this segment of the equity markets.

What does this mean for your return expectations?

In this article, we have considered the top-down picture. It is important to note that not all individual securities within any given asset class are necessarily expensive. Our bottom-up approach, which looks for quality assets that offer attractive real yields, is still yielding a number of investment opportunities. There are however fewer opportunities in the current environment, which is why we are holding cash.

We cannot predict the return you will earn from our portfolios over the medium term. However, we can recommend that you factor the following into your expectations:

- The market is not a coiled spring and there could be negative movements in the prices of shares and bonds.
- We hold large amounts of cash in our multi-asset class funds, which will help to buffer negative movements.
- Markets tend to overreact, so any normalisation could be extreme, offering us attractive buying opportunities.
- We have not participated in the mad rush for yield. We expect positive real returns from all the investments in our portfolios with the exception of cash.

To summarise, we cannot tell you exactly what time your teenager will be home, but for the next couple of nights, rather don't wait up. He might be late but rest assured – he is safe.

BIRDS OF A FEATHER? OUR INVESTMENT CASE FOR CAPITEC BANK

By Lisa Haakman

Lisa obtained an Hons.B. Acc from the University of Stellenbosch in 2000. While completing her articles at PricewaterhouseCoopers, she also completed her Higher Diploma in Taxation at the University of Cape Town, before going on to receive her CFA Charterholder qualification in 2006. Lisa also spent four years in London, working in treasury at Credit Suisse and in private equity and leveraged finance at RBS. Upon returning to South Africa in 2008, she worked as a sell-side analyst for five years, before joining PSG Asset Management in 2014 as an equity analyst.

Applying the 'duck test' to Capitec Bank leads to flawed conclusions

'If it looks like a duck, swims like a duck and quacks like a duck, then it probably is a duck.'

The 'duck test' is a form of inductive reasoning whereby you observe a subject's characteristics and then either draw conclusions about what it is; or counter-argue that it is not what it appears to be.

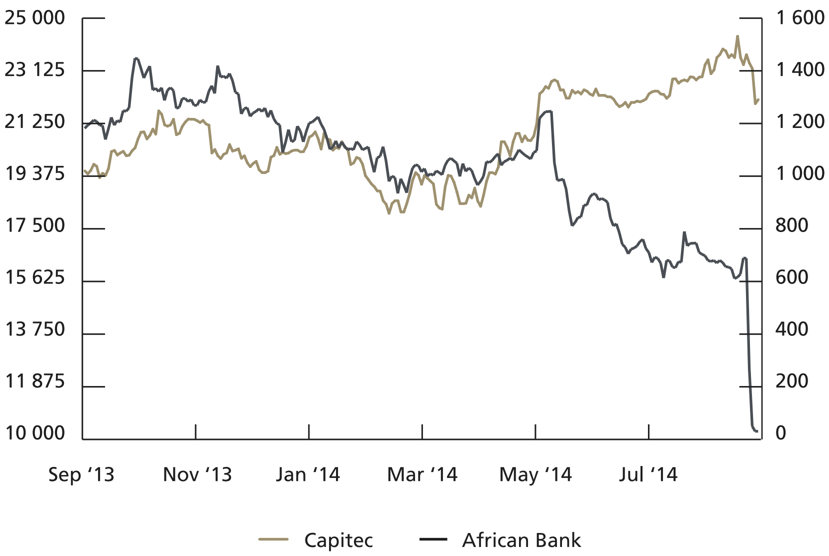
It is this type of logic that caused investors to treat African Bank and Capitec in a similar vein, and which resulted in their share prices moving in near tandem for two years before the African Bank demise (as shown in Graph 1).

It is this type of logic that resulted in Moody's downgrading Capitec's credit rating by two notches after African Bank was placed under curatorship. And it is this (often flawed) logic that gave us at PSG Asset Management an opportunity to build meaningfully on our Capitec position, both in equity and in credit, at a time when others were fearful.

Capitec has a strong competitive advantage

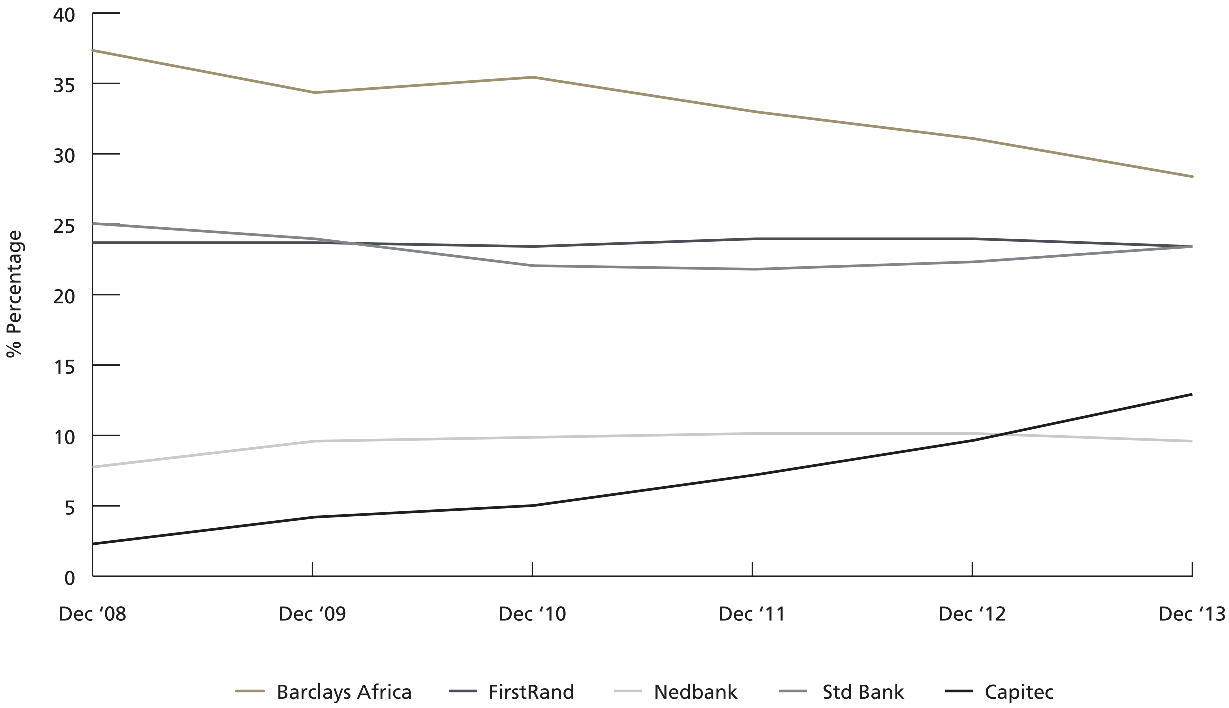
We do not view Capitec as an unsecured lender, but rather as one of the big five retail banks. However, Capitec operates with a lower cost structure relative to its big four peers and without legacy IT issues. This allows them to offer the most affordable banking product in South Africa, as confirmed by the recent September 2014 Solidarity Report, while operating at a cost-to-income ratio of only 34%, which is considerably lower than its peers. Despite acquiring

Graph 1: Relative share price performance of Capitec versus African Bank (September 2013 to July 2014)



Source: Bloomberg

Graph 2: Primary banked client market share in South Africa (December 2008 to December 2013)



Source: AMPS data

5.8 million clients since launching in 2002, Capitec is still gaining more than 100 000 customers per month with its compelling customer proposition.

An expanding product range is growing the target market

Capitec is expanding its product range. The bank now offers property finance through SA Homeloans, and is scheduled to launch a credit card in late 2015. This gives them a near-full suite of retail products, opening up their target market to include the upper LSM categories, which historically was the domain of the big four banks. While Capitec currently has a 13.1% market share of primary banked customers in South Africa (as shown in Graph 2), we believe management can comfortably reach their target of 20%.

We like the ethos of the company and the conservatism of management

Capitec's philosophy of affordability, simplicity and accessibility is unique in a South African context. Its honest, simple and transparent fee structures and bank branches that are open seven days a week have found resonance with consumers. Even more significant than this is the transparency and affordability of their products, which makes the bank defensive to regulatory scrutiny and changes. We are seeing an example of this now. While peers are smarting in the wake of a cap on credit life insurance, Capitec is smiling, as it has historically offered this to clients at zero charge, and will therefore see no impact on its earnings.

Capitec's conservatism is unrivalled in the industry, beginning with their credit granting, through to their provisioning, and finally culminating in their capital levels. Management currently operates the bank with provisions almost double their arrears (defined as only one missed instalment) and a capital adequacy ratio of 38%. Both of these ratios are more than double that of their closest peer.

This conservatism gives us confidence that when lesser mortals are cowering for shelter, Capitec will comfortably be weathering any storm that comes their way. In addition, being there for customers during turbulent times cements customer loyalty even further.

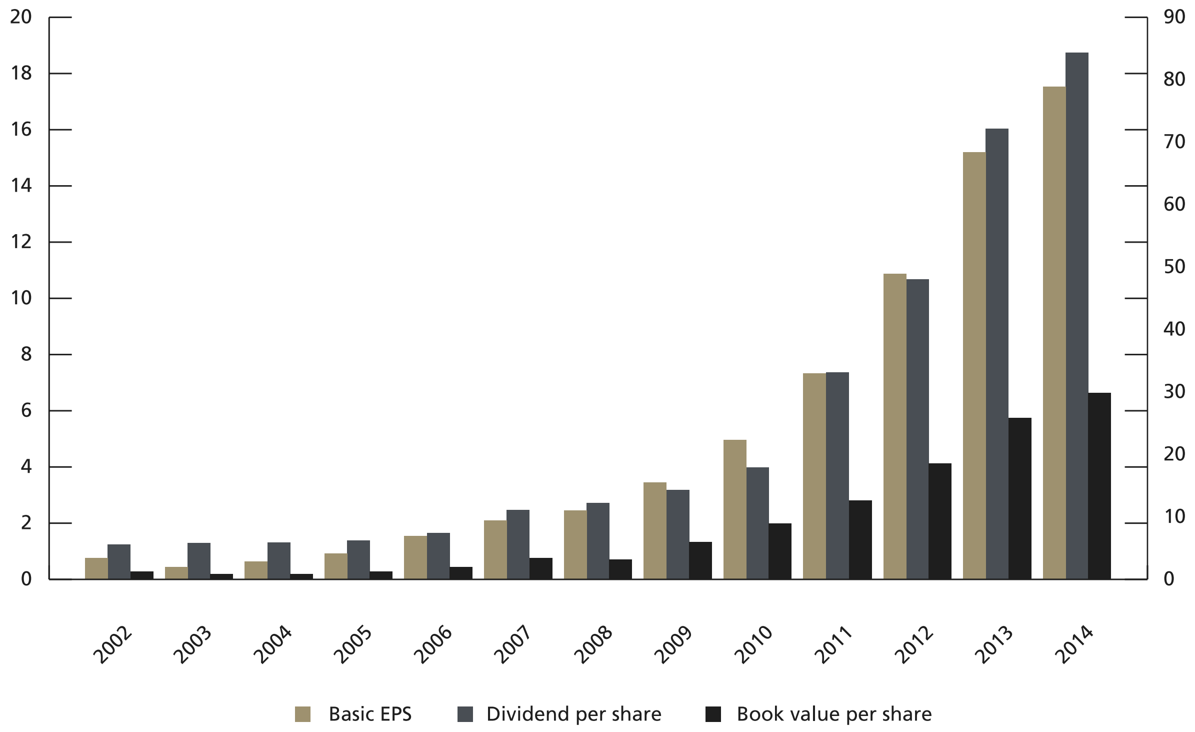
Management's interests are aligned with shareholders

As stipulated in the most recent annual report, management owns 19.9% of Capitec. This means that managers think like owners of the company and there is a strong alignment of interests with shareholders. The founder of Capitec, Riaan Stassen, retired at the end of 2013, but is still a non-executive director. His replacement, Gerrie Fourie, has been Head of Operations since inception and is a worthy successor. The Chairman, Michiel le Roux, has also been with the company since inception. Together, these individuals have a phenomenal track record of delivering value for shareholders. This is evidenced by the 30% compound annual growth rate in earnings per share (EPS), the 31% increase in dividend per share, and the 25% increase in book value per share over the last 12 years (as shown in Graph 3 on the next page).

The bank is enormously profitable

Despite an extraordinarily tough operating environment in South Africa, Capitec is currently the second most profitable bank globally by return on assets (ROA), as indicated in Table 1.

Graph 3: Capitec's earnings per share (EPS), dividend per share and book value per share growth (2002 to 2014)



Source: Bloomberg

Table 1: The 10 most profitable global banks

BANK	ROA 2014 ESTIMATE
Gentera	10.90%
Capitec Bank	5.08%
VZ Holding	4.86%
Inbursa	4.09%
Bank of Georgie	3.76%
Bank Rakyat Indonesia	3.41%
TBC Bank	3.40%
Shriram Transport Finance	3.14%
PT Bank	3.01%
Halyk Savings Bank	2.96%

Sources: UBS, PSG Asset Management

Management is running the bank at a conservative gearing of only 4.92 times, translating into a return on equity (ROE) of 25%, considerably above the median ROE for the big four banks.

We have not always owned Capitec in our funds

Although we have liked the Capitec business model for a number of years, it does not mean we have always owned it. We sold out of Capitec entirely in June 2011 (see Graph 4 on the next page) because we believed the margin of safety was insufficient relative to our internal intrinsic value of the company. The PSG Flexible Fund is shown in the graph for illustrative purposes, but serves as a proxy for our exposure to Capitec.

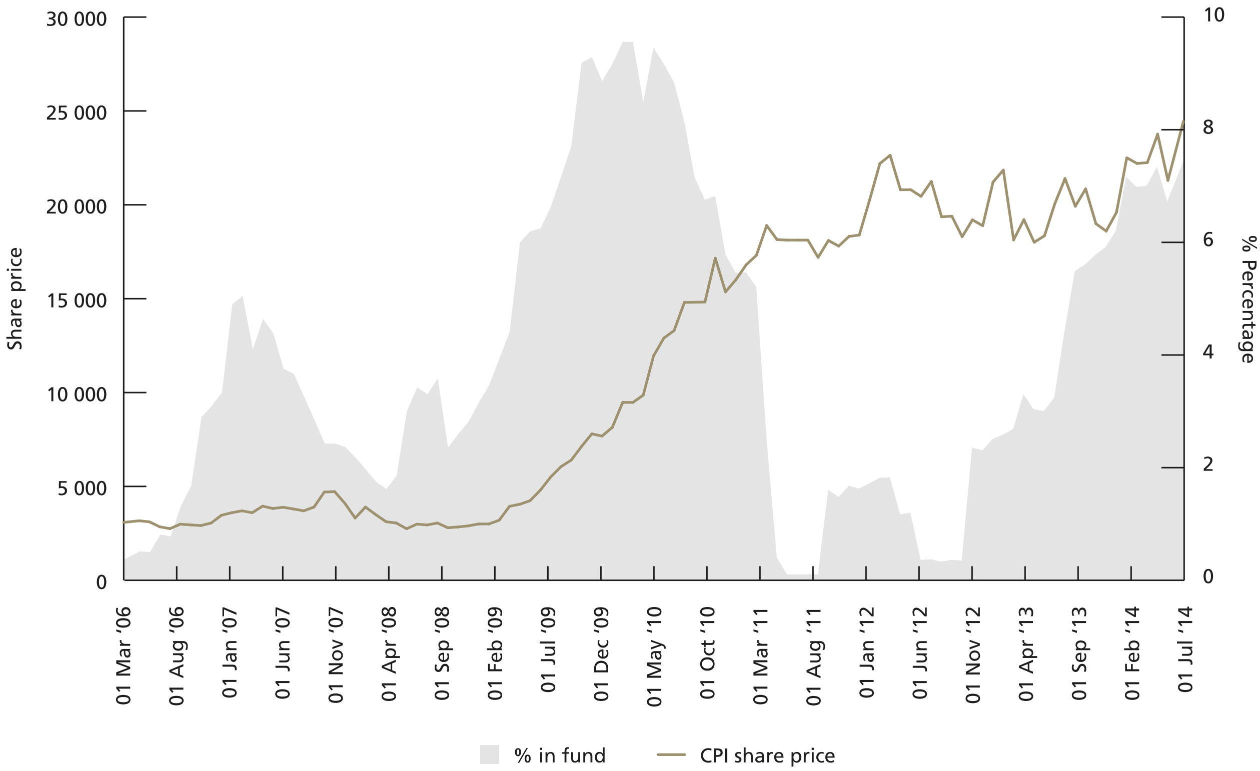
While earnings per share have steadily risen over the last three years, the price-earnings (P/E) ratio has declined to levels last seen in July 2009, as shown in Graph 5.

We believed earnings were also below normalised levels, and we saw this as a tremendous opportunity to increase the amount of Capitec we hold in your funds. In the weeks following African Bank being placed under curatorship and the double ratings downgrade by Moody's, we added to our holdings significantly. As at 30 September 2014, the PSG Flexible Fund held a 7.4% position in Capitec, the PSG Equity Fund a 5.7% position, and the PSG Balanced Fund a 5.4% position. We also increased our aggregate holding in Capitec credit in the PSG fixed income funds almost threefold.

We believe Capitec offers excellent return prospects for the coming years

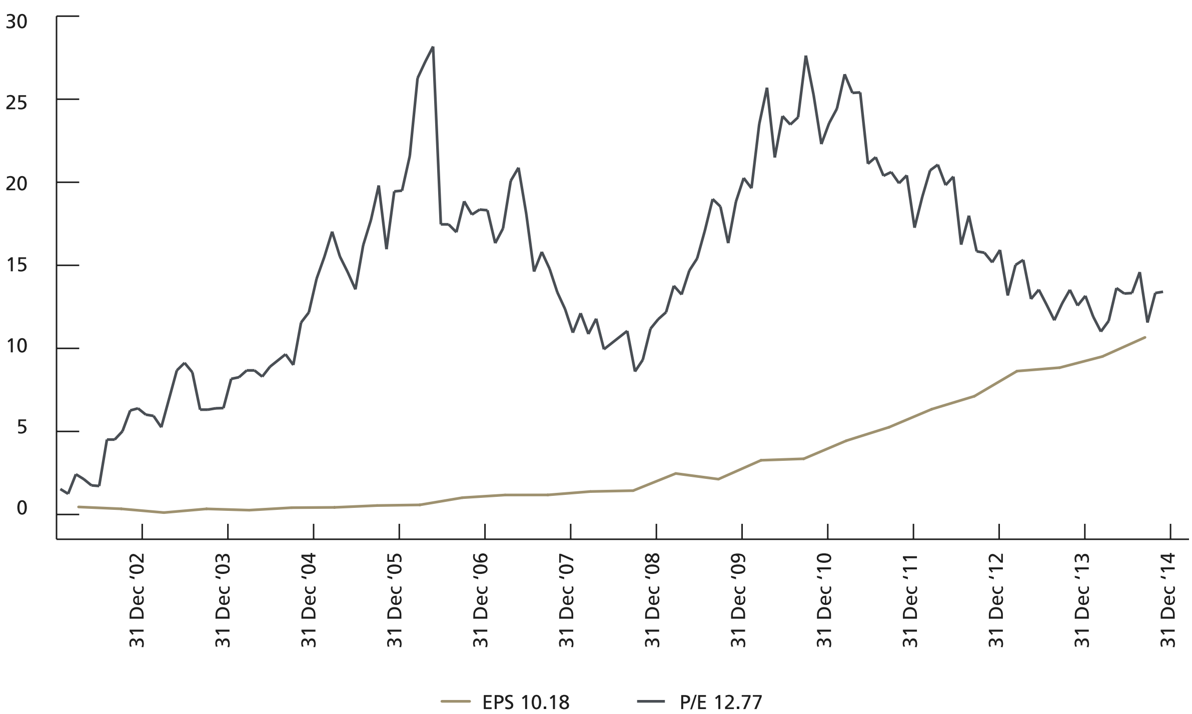
Capitec's interim results released on 29 September 2014 vindicated our contrarian view. The bank reported headline earnings growth of 21%, despite strengthening provisions against future credit impairments even further. Importantly, Capitec's reported credit loss ratio is well within through-the-cycle ranges where peers reported a marked deterioration in credit, evidence once again of their prudent credit granting.

Graph 4: PSG Flexible Fund holdings in Capitec (March 2006 to September 2014)



Source: PSG Asset Management

Graph 5: Capitec's price-earnings ratio relative to earnings per share (March 2002 to March 2014)



Source: Bloomberg

Despite a capital adequacy ratio of 38%, more than double what is required, Capitec succeeded in generating an ROE of 25% in a very tough economic cycle. The share still trades at an undemanding P/E ratio of only 12.7 times and a price-to-book ratio of 2.8 times. With its long runway for growth, we believe Capitec is an investment that will generate excellent returns for our fund holders in the coming years.

* PSG Asset Management's parent company, PSG Group Limited, holds a 28.3% stake in Capitec.

FUND FOCUS: THE PSG EQUITY FUND

Manager since 2002: Shaun le Roux

What has changed about the Fund and what has stayed the same over that time?

In the South African unit trust industry, it is unusual for a fund to have the same manager for more than 12 years. Over this period, little has changed. The PSG Equity Fund remains:

- invested in PSG Asset Management's (PSGAM's) high conviction ideas, that is, stocks that are thoroughly researched and undervalued
- benchmark agnostic
- focused on seeking to exploit opportunities from as wide a universe as possible
- focused on long-term investment ideas

We have made mistakes over this period. We sought to learn from those mistakes and, where necessary, enhance our investment process. For example, we erred in 2008 by being invested in some low quality businesses with high earnings, and some of these fared poorly during the crisis. As a result, our selection process today insists on a much higher margin of safety as well as confidence that earnings are below normal levels before we commit capital to such opportunities.

We added significantly to the depth of our research capability over recent years and now have a team of ten investment professionals engaged in equity research. With our global equity research process, the PSG Equity Fund has been investing directly offshore for more than three years. Investing offshore has enabled us to:

- widen our universe
- deepen our knowledge
- diversify our portfolios
- exploit the best opportunities to buy mispriced quality businesses around the world.

What are the Fund's benchmark and objectives?

The benchmark is the FTSE/JSE All Share Index (ALSI). The Fund does not own stocks just because they are a significant holding in the benchmark. All of our portfolio positions are held on their own merit.

The Fund seeks to outperform its benchmark and be a top-quartile performer within the peer group over an appropriate investment period, but no less than three years.

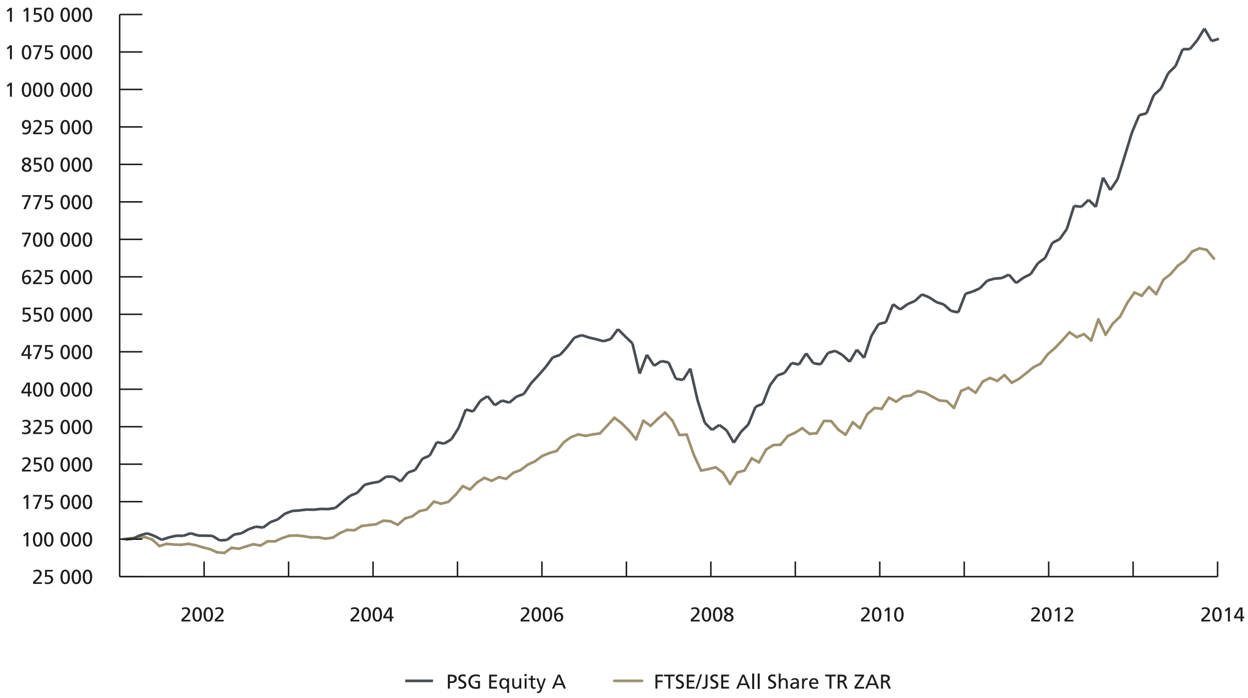
How do we construct the portfolio?

PSGAM has a Buy List of stocks that we believe have a high probability of generating superior investment returns over the long term. The portfolio manager selects stocks from the Buy List and ensures that risk is being adequately controlled, specifically that the Fund is appropriately diversified and free of unintended macro bets.

What types of stocks does PSGAM typically invest in?

Our highest conviction ideas are generally high quality businesses trading for less than what we think they are worth. Quality is determined by having an enduring competitive advantage, or moat, and a strong, incentivised management team. Opportunities to invest in high quality businesses that are cheap typically occur when the market is concerned about temporary

Graph 1: The PSG Equity Fund outperformed its benchmark over the past 12 years



Source: Morningstar

circumstances that do not affect the long-term value of a company. Exploiting such opportunities requires a contrarian mindset and a willingness to take a long-term view.

We also invest in lower quality businesses, but only when we are confident that the margin of safety is high and the likelihood of permanent capital loss is low.

Are PSGAM growth or value managers?

We do not have a pigeon-holed investment style. We seek to own companies that are trading for less than we think they are worth, whether they are high quality growth stocks or lower quality value opportunities. We don't own overpriced stocks and only own low quality businesses when there is a wide buffer or margin of safety.

How does the portfolio look today?

Despite the strong run in equity markets over the past few years, we continue to find high conviction investment opportunities in equities. This is especially the case abroad and the likes of Markel, Brookfield and J.P.Morgan are currently top ten holdings.

The stocks that we own on behalf of our investors are attractively priced and as a result, the price-earnings (P/E) ratio of the Fund (at 12.6 times) is materially less than the P/E ratio of its benchmark, the ALSI (at 17.1 times). This is despite the fact that we believe that the companies we own are at least the same quality as the average stock on the JSE. The assets we manage are of a size that allows us to invest outside of the Top 40. For example, Capitec and Adcorp are currently top ten holdings in the Fund, even though they are not in the Top 40.

Who should and shouldn't invest in the Fund?

Investors in an equity product should have a long-term investment horizon, typically at least five years. If they are able to stomach market volatility and infrequent but sometimes sharp equity market drawdowns, they should enjoy the superior capital growth that a well-constructed equity product provides. For example, the PSG Equity Fund has beaten inflation by approximately 15% per year over the past 12 years.

Investors in the PSG Equity Fund should anticipate short-term underperformance from time to time. Furthermore, the Fund can look very different to the benchmark and many peer group portfolios when the best opportunities lie outside the Top 40.

The PSG Equity Fund continues to outperform its benchmark and ranks highly amongst its peers

As shown in Graph 1, R100 000 invested in the PSG Equity Fund in 2002 is worth R1 100 000 today, even after factoring in all costs. The same amount invested in the ALSI would be worth R660 000. The PSG Equity Fund has compounded its value by 4.7% per year faster than the ALSI over this period. The Fund continues to rank in the top 10% in its category over three years, five years and since inception.

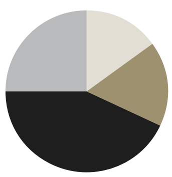
PORTFOLIO HOLDINGS AS AT 30 SEPTEMBER 2014

PSG Equity Fund

Top 10 equities

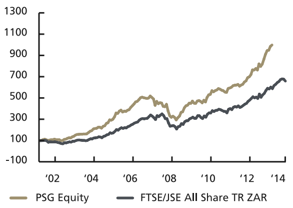
Steinhoff International Holdings Ltd
Glencore Xstrata Plc
Capitec Bank Holdings Ltd
International Business Machines Corp
Old Mutual
Markel Corp
Anglo American Plc
Adcorp Holdings Ltd
JP Morgan Chase & Co
Brookfield Asset Management

Asset allocation



Resources	15%
Financials	17%
Industrials	43%
Domestic equity	**75%**
Foreign equity	25%
Total	**100%**

Performance

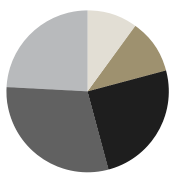


PSG Flexible Fund

Top 10 equities

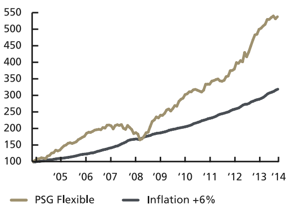
Steinhoff International Holdings Ltd
Capitec Bank Holdings Ltd
Berkshire Hathaway Inc
J Sainsbury Plc
Sasol Ltd
Anglo American Plc
Super Group Ltd
International Business Machines Corp
AVI Limited
EOH Holdings Limited

Asset allocation



Resources	10%
Financials	11%
Industrials	25%
Domestic equity	**46%**
Domestic cash	30%
Foreign equity	24%
Total	**100%**

Performance

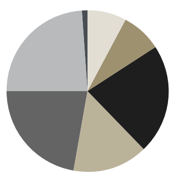


PSG Balanced Fund

Top 10 equities

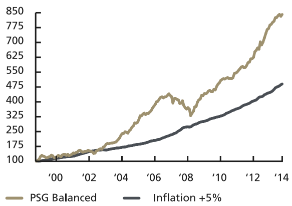
Steinhoff International Holdings Ltd
Capitec Bank Holdings Ltd
Berkshire Hathaway Inc
Super Group Ltd
Anglo American Plc
International Business Machine Corp
J Sainsbury Plc
Sasol Ltd
Microsoft Corp
Glencore Xstrata Plc

Asset allocation



Resources	8%
Financials	8%
Industrials	22%
Domestic equity	**38%**
Domestic bonds	15%
Domestic cash	22%
Foreign equity	24%
Foreign cash	1%
Total	**100%**

Performance



PSG Stable Fund

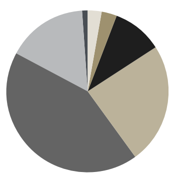
Top 5 equities

Steinhoff International Holdings Ltd
Capitec Bank Holdings Ltd
International Business Machine Corp
Berkshire Hathaway Inc
J Sainsbury Plc

Top 5 bond issuer exposures

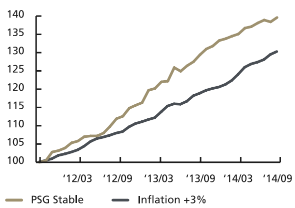
Capitec Bank Ltd
Standard Bank Ltd
Firstrand Bank Ltd
Landbank Ltd
The Thekwini Fund 11 (RF) Ltd

Asset allocation



Resources	3%
Financials	3%
Industrials	10%
Domestic equity	**16%**
Domestic bonds	24%
Domestic cash	43%
Foreign equity	16%
Foreign cash	1%
Total	**100%**

Performance



PSG Diversified Income Fund

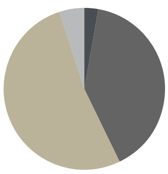
Top 5 equities

Berkshire Hathaway Inc
Capitec Bank Holdings Ltd
International Business Machine Corp
Steinhoff International Holdings Ltd
Microsoft Corp

Top 5 bond issuer exposures

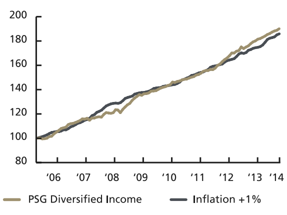
Nedbank Ltd
Mercedes-Benz South Africa Ltd
Capitec Bank Ltd
Standard Bank Ltd
Landbank Ltd

Asset allocation



Domestic equity	3%
Domestic cash	40%
Domestic bonds	52%
Foreign equity	5%
Total	**100%**

Performance

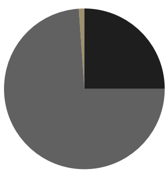


PSG Income Fund

Top 10 bond issuer exposures

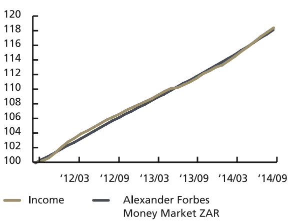
Absa Bank Ltd
Capitec Bank
Nedbank Ltd
Standard Bank
Bidvestco Ltd
Barloworld Ltd
Firstrand Bank Ltd
Landbank Ltd
Netcare (Pty) Ltd
Steinhoff Services (Pty) Ltd

Asset allocation



Fixed rate notes	25%
Floating rate notes	74%
Cash & NCD's	1%
Total	**100%**

Performance

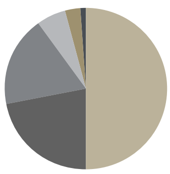


PSG Global Equity Fund IC Limited

Top 10 equities

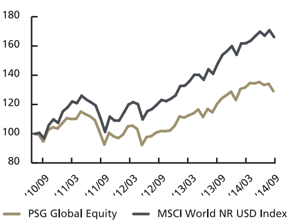
International Business Machines Corp
Berkshire Hathaway Inc
Markel Corp
J Sainsbury Plc
Steinhoff International Holdings Ltd
JP Morgan Chase & Co
Capital One Financial Corp
Porsche Automobil Holdings - Preferred
Brookfield Asset Management
Cisco Sysems Inc

Regional allocation



US	50%
Europe	22%
UK	18%
Africa	6%
Cash	3%
Asia	1%
Total	**100%**

Performance

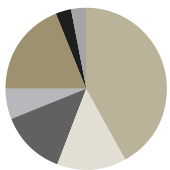


PSG Global Flexible Fund IC Limited

Top 10 equities

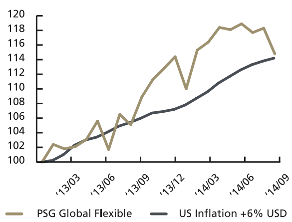
International Business Machines Corp
Markel Corp
Berkshire Hathaway Inc
Steinhoff International Holdings Ltd
J Sainsbury Plc
JP Morgan Chase & Co
Capital One Financial Corp
Porsche Automobil Holdings - Preferred
Brookfield Asset Management
Cisco Sysems Inc

Regional allocation



US	42%
Europe	14%
UK	13%
Africa	6%
Cash	19%
Asia	3%
Canada	3%
Total	**100%**

Performance



PERFORMANCE TO 30 SEPTEMBER 2014

FUND PERFORMANCE								
		1 YEAR			2 YEARS**			
FUND	FUND SIZE	RETURN	SECTOR RANK	SECTOR COUNT	RETURN	SECTOR RANK	SECTOR COUNT	
LOCAL FUNDS								
PSG Equity A	R 1 954 233 662	20,46	3	121	28,88	1	108	
PSG Equity A BM (JSE All Share TR)		15,45	51	122	21,08	34	109	
PSG Flexible	R 5 498 418 297	15,19	15	72	22,50	6	65	
PSG Flexible BM: CPI +6%		12,46	35	73	12,45	45	66	
PSG Balanced A	R 3 743 369 542	12,96	37	104	18,39	17	95	
PSG Balanced BM: CPI +5%		11,44	67	105	11,43	89	96	
PSG Stable	R 1 803 368 827	7,96	70	90	11,36	41	87	
PSG Stable BM: CPI+3%		9,43	44	91	9,42	68	88	
PSG Diversified Income	R 719 428 893	6,92	16	58	7,98	6	54	
Alexander Forbes Short Term Fixed Interest Index		7,04	14	59	7,22	9	55	
PSG Income	R 54 290 215	6,62	19	58	5,41	17	54	
Alexander Forbes Money Market Index		5,65	41	59	5,42	46	55	
PSG Money Market A	R 2 605 325 007	5,53	13	28	5,26	17	27	
South African IB Money Market Mean		5,54	13	29	5,33	12	28	
PSG Global Equity Feeder Fund	R 153 522 067	19,53	21	28	29,32	20	24	
MSCI World NR USD		25,98	3	29	35,93	4	25	
PSG Global Flexible Feeder Fund A	R 467 361 130	17,64	8	18				
PSG Global Flexible BM: US Inflation +6%		20,93	5	19				
OFFSHORE FUNDS								
PSG Global Equity	$ 38 806 493	7,35	438	540	12,64	271	484	
MSCI World NR USD		12,21	224	541	16,15	97	485	
PSG Global Flexible Fund	$ 101 648 930	5,35	43	94				
US CPI +6%		7,71	19	95				

* Manager inception dates
** Annualised (for periods greater than 12 months)
All the performance data is net of fees, for a lump sum, includes income, and assumes reinvestment of income on a NAV to NAV basis.

	3 YEARS**			5 YEARS**			10 YEARS**			INCEPTION*			
	RETURN	SECTOR RANK	SECTOR COUNT	RETURN	SECTOR RANK	SECTOR COUNT	RETURN	SECTOR RANK	SECTOR COUNT	INCEPTION DATE	RETURN	SECTOR RANK	SECTOR COUNT
	25,70	5	98	20,51	3	85	19,36	11	45	01/03/2002	20,99	2	39
	22,17	28	99	18,01	17	86	18,77	13	46		16,26	29	40
	19,47	22	61	18,98	8	55	18,47	2	14	01/11/2004	18,48	2	14
	11,95	44	62	11,35	38	56	12,26	10	15		12,29	9	15
	17,21	26	85	15,23	13	62	14,88	12	27	01/06/1999	15,44	4	12
	10,94	79	86	10,33	59	63	11,08	26	28		10,70	11	13
	11,63	40	77							13/09/2011	11,58	42	76
	8,94	68	78								8,94	67	77
	8,04	9	45	7,18	23	38				10/04/2006	7,87	11	22
	6,80	23	46	6,25	34	39					7,53	14	23
	5,72	19	45	6,55	30	38	8,18	10	16	01/09/2011	5.60	5	7
	5,49	41	46	5,38	36	39	6,94	16	17		5.50	8	8
	5,29	18	27	5,74	14	26	7,32	6	17	19/10/1998	8,82	4	6
	5,37	12	28	5,80	8	27	7,33	6	18		8,82	5	7
	22,22	20	22							03/05/2011	18,40	20	21
	32,09	3	23								27,12	3	22
										10/04/2013	25,60	6	16
											26,67	6	17
	11,72	355	439							23/07/2010	6,30	314	385
	17,92	74	440								12,90	36	386
										01/01/2013	8,23	17	80
											7,92	22	81

UNIT TRUST SUMMARY

	SOUTH AFRICAN PORTFOLIOS							RAND-DENOMINATED OFFSHORE	
	PSG Equity Fund	**PSG Flexible Fund**	**PSG Balanced Fund**	**PSG Stable Fund**	**PSG Diversified Income Fund**	**PSG Income Fund**	**PSG Money Market Fund**	**PSG Global Flexible Feeder Fund**	**PSG Global Equity Feeder Fund**
Fund Category (ASISA classification)	South African - Equity - General	South African - Multi Asset - Flexible	South African - Multi Asset - High Equity	South African - Multi Asset - Low Equity	South African - Multi Asset - Income	South African - Interest Bearing - Short-term	South African - Interest Bearing-Money Market	Global - Equity - General	Global - Multi Asset - Flexible
Investment Objective	Provide outstanding capital growth and deliver consistent upper quartile returns within an acceptable risk profile.	Achieve superior medium- to long-term capital growth through exposure to selected sectors of the equity, bond and money markets.	Provide long-term capital growth and a reasonable level of income.	Generate a return of CPI + 3% over a rolling three-year period after costs, while aiming to achieve capital appreciation with low volatility and low correlation to equity markets through all market cycles.	Preserve capital and maximise income returns.	Maximise income and preserve capital while achieving long-term capital appreciation as interest rate cycles allow.	Obtain a high level of income as is consistent with capital preservation and liquidity.	Outperform the average of the world's equity markets, as represented by the MSCI World Free NR USD Index (in ZAR).	Achieve superior medium- to long-term capital growth through exposure to selected sectors of the global equity, bond and money markets.
Benchmark	FTSE/JSE All Share Index after costs	Inflation +6%	Inflation +5%	Inflation +3% over rolling 3-year period after costs	Inflation +1%	Alexander Forbes Money Market Index after costs	South African - Interest Bearing - Money Market Mean	MSCI World Free NR USD Index (in ZAR)	US Inflation + 6%
Risk Rating	High	Moderate - High	Moderate - High	Moderate	Low - Moderate	Low - Moderate	Low	High	Moderate - High
The Fund is suitable for:	Investors who: • Seek an equity-focused portfolio that has outstanding growth potential • Aim to maximise potential returns within an acceptable risk profile • Focus on a long-term investment horizon	Investors who: • Seek exposure to the equity market but with managed risk levels • Aim to build wealth • Focus on a medium- to long-term investment horizon	Investors who: • Would prefer the fund manager to make the asset allocation decisions • Aim to build wealth within a moderate risk investment	Investors who: • Have a low risk appetite but require capital growth in real terms • Focus on a short- to medium-term investment horizon	Investors who: • Have a low risk appetite and with an income requirement • Want to earn an income, but need to try and beat inflation • Focus on a short- to medium-term investment horizon	Investors who: • Have a low risk appetite with an income requirement • Focus on a short- to medium-term investment horizon	Investors who: • Seek capital stability, interest income and high liquidity through a low- risk investment • Need an interim investment vehicle or 'parking bay' for surplus funds • Focus on a short- to medium-term investment horizon	Investors who: • Seek an equity-focused portfolio that has outstanding growth potential • Aim to maximize potential returns within a moderate risk investment • Focus on a long-term investment horizon	Investors who: • Want a managed solution in offshore markets • Want to diversify their holdings across the world • Focus on a medium-to long-term investment horizon
Net Equity Exposure	100%	0-100%	0-75%	0-40%	0-10%	0%	0%	100%	40-75%
Income Distribution	Bi-annually	Bi-annually	Bi-annually	Bi-annually	Quarterly	Quarterly	Monthly	Annually	Annually
Minimum Investment	R2 000 lump sum, or R250 monthly debit order	R2 000 lump sum, or R250 monthly debit order	R2 000 lump sum, or R250 monthly debit order	R2 000 lump sum, or R250 monthly debit order	R2 000 lump sum, or R250 monthly debit order	R2 000 lump sum, or R250 monthly debit order	R25 000 lump sum	R2 000 lump sum	R2 000 lump sum
Fees	Annual Management Fee: Class A: 1.71% Class B: 1.14% + 22.8% of outperformance of Benchmark	Annual Management Fee: Class A: 1.14% + 7.98% of outperformance of High Watermark	Annual Management Fee: Class A: 1.71% Class B: 1.14% + 7.98% of outperformance of High Watermark	Annual Management Fee: Class A: 1.71%	Annual Management Fee: Class A: 1.14%	Annual Management Fee: Class A: 0.74%	Annual Management Fee: Class A: 0.57% Class B: 0.23%	Annual Management Fee: Class A: 0.86%	Annual Management Fee: Class A: 0.86% Class B: 0.29%
Total Expense Ratio*	Class A: 1.75% Class B: 2.10%* included in TER a Performance Fee of: 0.92%	Class A: 2.47%* included in TER a Performance Fee of: 1.31%	Class A: 1.74% Class B: 2.13%* Included in TER a Performance Fee of: 0.97%	Class A: 1.78% included in TER a Performance Fee of: 0.09%	Class A: 1.19%	Class A: 1.14%	Class A: 0.59%	Class A: 2.22%	Class A: 2.33%
Compliance with Prudential Investment Guidelines (Regulation 28)	No	No	Yes	Yes	Yes	Yes	Yes	No	No

Please note that the portfolios have Total Expense Ratios (TER's) as listed above. For the period from 1 October 2013 to 30 September 2014 on an annualised basis, the above percentages of the average Net Asset Value of the portfolios were incurred as charges, levies and fees. A Higher TER ratio does 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 TER's.

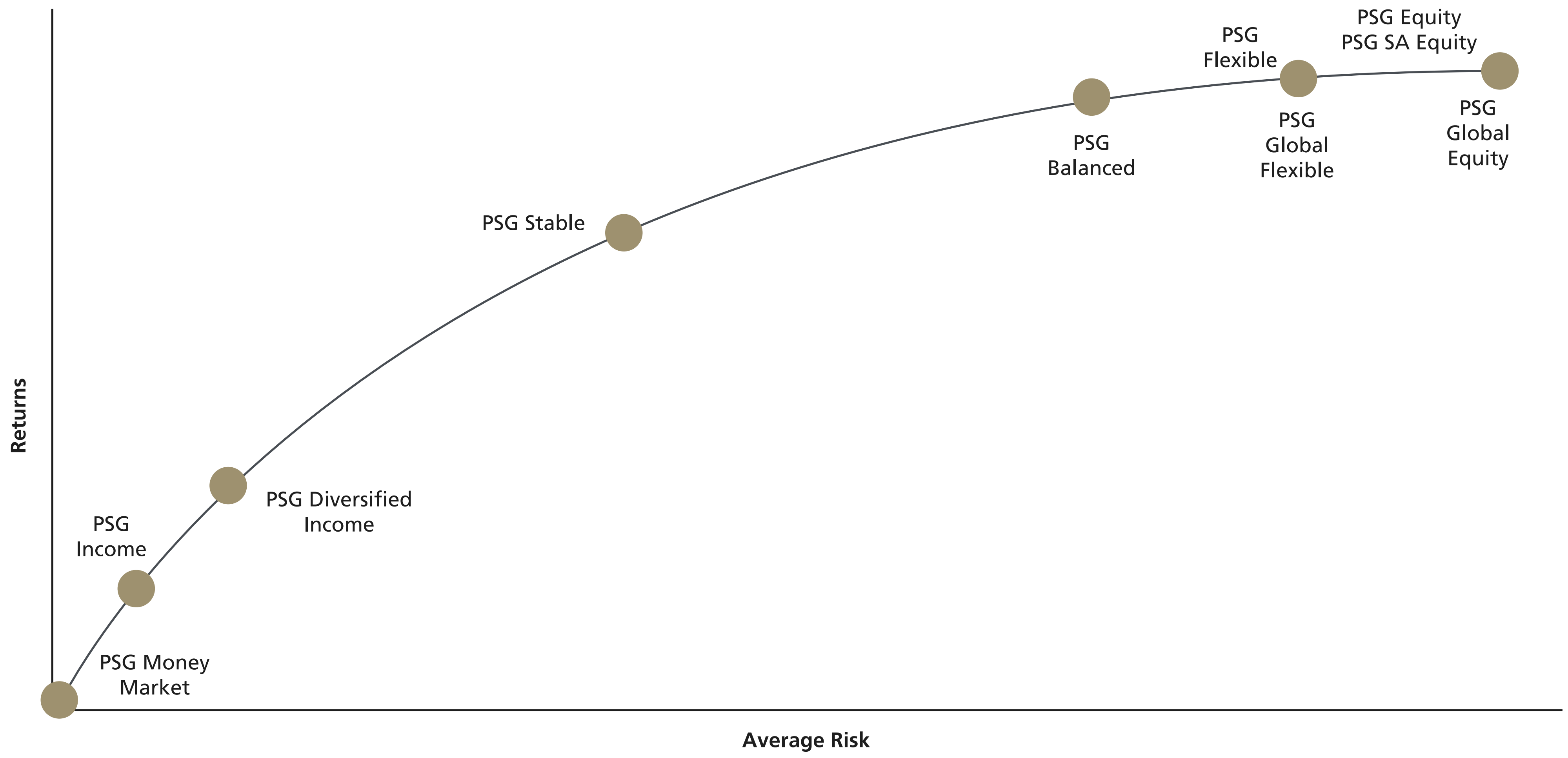
* Included in the TER's a performance fee of the Net Asset Value of the participatory interest of the portfolio as above.

** Total Expense Ratio (TER) for this class of participatory interest cannot be accurately determined due to the fund class being less than 12 months in existence. The TER of this class of participatory interest will be higher than the quoted service charge of the manager.

Collective Investment Schemes in Securities (CIS) are generally medium to long-term investments. The value of participatory interests (units) may go down as well as up and past performance is not a guide to the future. CIS are traded at ruling prices and can engage in borrowing and script lending. Fluctuations or movements in the exchange rates may cause the value of underlying international investments to go up or down. A schedule of fees and charges and maximum commissions is available on request from PSG Collective Investments Limited. Commission and incentives may be paid and if so, are included in the overall costs. Forward pricing is used. The portfolios may be capped at any time in order for them to be managed in accordance with their mandate. Different classes of Participatory Interest can apply to these portfolios and are subject to different fees and charges. PSG Collective Investments Limited is a member of the Association of Savings and Investments South Africa (ASISA).

Conflict of Interest Disclosure: The Fund may from time to time invest in a portfolio managed by a related party. PSG Collective Investments or the Fund Manager may negotiate a discount in fees charged by the underlying portfolio. All discounts negotiated are re-invested in the Fund for the benefit of the investor. Neither PSG Collective Investments Limited nor the Fund Manager retains any portion of such discount for their own accounts. PSG Asset Management (Pty) Ltd (FSP no 29524) and PSG Collective Investments Limited are subsidiaries of PSG Group Limited. The Fund Manager may use the brokerage services of a related party, PSG Securities Ltd.

RISK/RETURN PROFILE



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