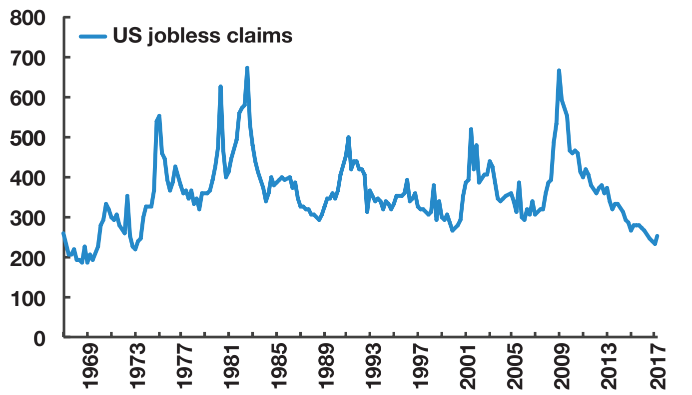
INVESTMENT STRATEGY

Q2 | 2017

THE ECONOMY

- US jobless-benefit rolls decline to a 28-year low.
- Oil falls below US$50 a barrel.
- France's PMI hits a 6-year high, now exceeding that of Germany.
- Germany's IFO current conditions index reaches a 50-year high.
- GDP in the Euro area rises 0.6% q/q to March 2017.
- UK inflation lifts to 2.9%, the highest in 4 years.
- SA posts a trade surplus of R11.44bn for March 2017.
- SA's foreign exchange reserves drop to $39bn as rand weakening is offset by government's forex payments.
- SA unemployment increases to 27.7% - the highest figure since 2003.
- SA enters a recession as GDP contracts by 0.7% in Q2 after the previous quarter's 0.3% contraction.
- The RMB business confidence falls to 29 points – a level last seen in 2009.
- SA inflation drops to 5.1% y/y in June.

The sharp fall in US jobless claims

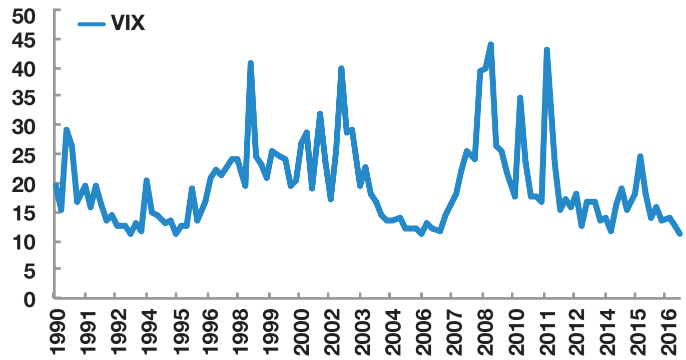


Source: Bloomberg | June 2017

EQUITIES

- The Nasdaq climbs above 6000 for the first time and S&P 500 hits record high.
- Good results by Alphabet and Amazon push the Nasdaq even higher.
- The FTSE 100 and Frankfurt's Dax 30 touch new highs.
- Continental Europe outperforms its developed country peers in Q2 and the CAC 40 hits a 9-year high.
- The VIX 'fear index' reaches 25-year lows.
- The largest SA-listed stock, Naspers, hits an all-time high.
- The 3rd draft of the Mining Charter punishes mining stocks.
- Barclays places Absa shares on the market in the largest bookbuild in the history of the JSE.
- The ALSI declines 0.4% during Q2 on a total return basis.
- The MSCI World Index (US$) returns 4.0% on a total return basis.
- Emerging markets have another strong quarter giving 6.4% in US$ terms.

Markets return to 'risk on'

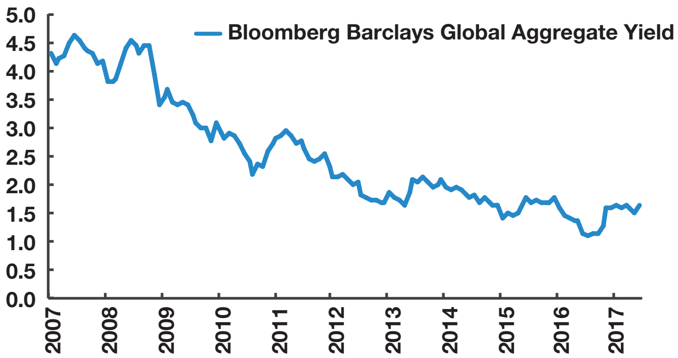


Source: I-Net | June 2017

FIXED INCOME

- The Fed raises the federal funds target rate to 1-1.25%.
- Gobal bonds rose 2.6% over the quarter.
- The ECB drops its guidance that rates may fall further; it now expects borrowing costs to stay at current levels.
- Moody's downgrades China's credit rating from Aa3 to A1.
- S&P downgrades SA local currency debt to one notch above junk and foreign currency to junk.
- Fitch downgrades SA local and foreign currency debt to junk.
- Moody's downgrades SA local and foreign currency debt to one notch above junk and downgrades 5 SA banks.
- SA nominal bonds gain 1.5% during Q2.
- Locally the benchmark R186/10-year bond ends Q2 6 bps lower.
- SA inflation-linked bonds add 1.0% vs. the 1.9% from cash.
- Local listed property returns 3.6% for the quarter.

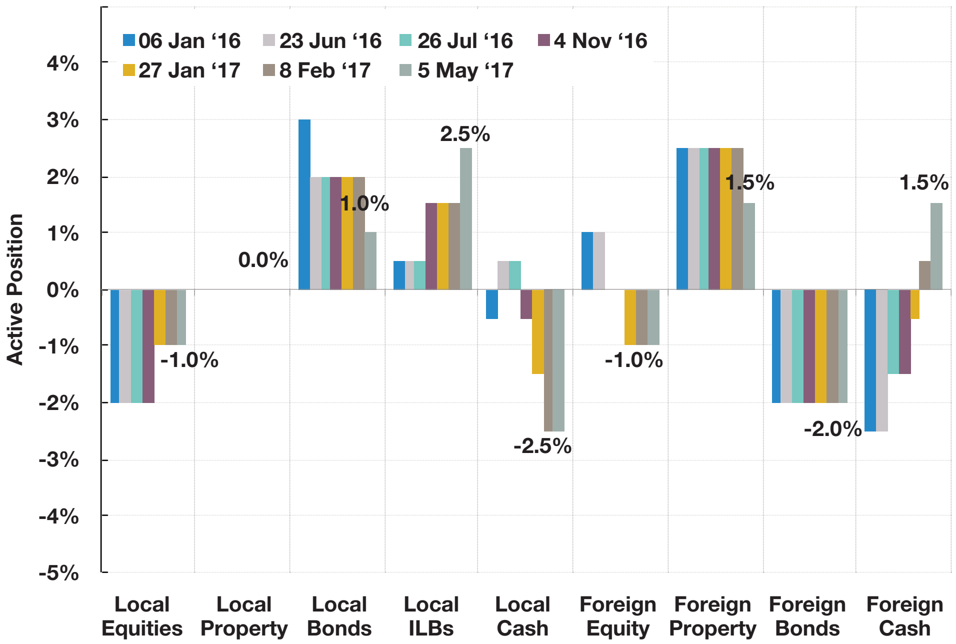
Global bond yields slow to rise



Source: I-Net | June 2017

Investments

SIM ASSET ALLOCATION | Jan 2016 to Jun 2017



During Q2 2017

- In May we decreased our overweight position in SA conventional bonds by 1% in favour of SA inflation-linked bonds, as we believe SA now requires a higher inflation risk premium and a prospective real return of 2% on conventional bonds is no longer sufficient.
- We also decreased our overweight position in global property companies by 1% in favour of European cash, as the euro is two standard deviations cheaper versus the US dollar.

Source: Sanlam Investments (June 2017)

DOMESTIC	POSITION	RATIONALE
Local equities	Underweight	We remain underweight equities, with the SWIX trading on a current price to earnings (PE) ratio of about 15.5. Given earnings forecasts the PE ratio could drop to about 13.5 in a year's time, still above fair value, but companies which derive their earnings from SA have become cheap.
Local bonds	Overweight	We reduced our overweight in SA long bonds as, with the increased political uncertainty, investors in SA bonds need a higher inflation risk premium. The real yield of 3% remains attractive relative to that of the bonds of similarly rated countries – hence we keep a small overweight.
Inflation-linked bonds	Overweight	We increased our overweight position, as ten-year inflation-linked bonds (ILBs) currently offer an attractive real yield of 2.50%. SA ILBs provide protection against unexpected inflation and are currently attractive relative to developed market (DM) ILBs.
Local listed property	Neutral	We believe JSE-listed properties are slightly expensive at a current dividend yield of 7.4%, but retained our neutral position for geographic diversification and its higher yield in a yield-starved environment. Approximately 35% of JSE-listed property companies' earnings are now from outside SA.

INTERNATIONAL	POSITION	RATIONALE
Global equities	Underweight	We maintain our underweight as the US market is expensive in our opinion. In fact, the Graham & Dodd P/E multiple for the US has only been higher during the internet bubble of the 90s and the run-up to the US stock market crash of 1929. But European equities remain cheap and we continue to hold an overweight position in Europe.
Global bonds	Underweight	We retained our underweight position. We would require a premium above long-run global inflation assumptions of 2% before investing in DM government bonds.
Global property	Overweight	We reduced the size of our overweight position in our basket of DM REITs. We retain an overweight, though, as the average dividend yield of our basket of properties is 5.5%.