# News and Review

**Volume Two – April 2016**

Dear Investor

We have come to a stage in the lifecycle of our portfolio of Unit Trusts where, after careful consideration, we have made the decision to close all portfolios under management that are smaller than R50 million. This decision comes as a result of new legislation with regards to Unit Trusts recently introduced by the Financial Services Board. In context of the South African Unit Trust industry, this legislation stipulates that portfolios below R50 million in size are not considered to be viable investment options, and it further stipulates that the management company of the portfolios - in this case Itransact Fund Managers (IFM) - must keep additional capital reserves for each portfolio below R50 million. The two portfolios that were affected by this decision were the IFM Income Provider and the IFM Dynamic Fund.

As a result of this additional capital requirement the decision was taken to amalgamate these two smaller portfolios with the IFM Balanced Value Fund of Funds. This action will result in reduced costs for investors in the two smaller portfolios due to improved economies of scale, and furthermore will allow IFM to provide a better focus on the remaining portfolios under management. Accordingly, we believe that the amalgamation will be beneficial for all our investors.

Detailed communication in this regard was sent to all investors in the three funds affected. The amalgamation process will be finalized on the 31st of May, with the special distribution of the units reinvested in the IFM Balanced Value Fund of Funds effective on 1 June 2016.

All investors are reminded to ensure that they have updated their FICA details with IFM within the last 12 months. This information is very important, as no enquiry or request may be undertaken by a client consultant unless the correct updated detail is on file with us. The necessary requirement for South African citizens is to send our team a copy of their identification document, for example a ID book or passport, written confirmation of the residential address and contact particulars of the person e.g. utility bill (not older than 3 months) reflecting the name and address of the person and a copy of a cancelled cheque or recent bank statement with the account name and bank account details (the bank account must be in the name of the investing party, no third party accounts or payments are permitted). Note that we may not accept an electronic generated statement as proof of bank account verification - the account document must have a bank stamp on it.

Itransact Fund Managers (RF) (Pty) Ltd
15 Philips Street, Ferndale, Randburg, South Africa, 2194 | PO Box 4769, Randburg, South Africa, 2125
Tel: 0861 11 60 75 | Fax: 011 561 6812
Company Registration Number: 1999/012170/07
Directors: CM Gill [Managing], JF Zwarts [Chairman], MR Baisley, TC Meyer, J Solms, JE van Heerden
Secretary: Aspen Company Services
Fund Manager: Heiden Grimaud Asset Management (Pty) Ltd (FSP 596)

As mentioned in our previous newsletter, we now offer all our investors the opportunity to log onto IFM's online enquiry portal - IBrowse. This functionality will provide you, as investor, with the ability to effect instructions, such as the generation of statements without having to contact a consultant. Should you wish to make use of this functionality, kindly contact the IFM client consultant team for assistance on how to register as a system user. The consultant will guide you through a few easy steps and no charges are incurred.

Any enquiries regarding your investments can be directed as follows:

- All administrative enquiries, for example a request of statement or balance of investment, redemption request, update of contact details, enquiries regarding FICA or assistance required to log onto the IBrowse system is handled by Itransact Fund Managers. The telephone number is 0861 11 60 75, and email is admin@itransactfm.co.za.

- All investment specific or portfolio enquiries are handled by Heiden Grimaud Asset Management. The telephone number for the fund is 0861 378 378, and the email is investments@heidengrimaud.co.za.

## News from our Fund Manager

HeidenGrimaud
Asset Management

### 1. <u>How do we decide which investments to make?</u>

Imagine yourself transported back hundreds of years to a small village in the countryside. You find yourself strolling through a market, which is a hive of activity, Goods and services of every description are being bought and sold with money exchanged for these. It is the free enterprise system - capitalism in motion. Some merchants are doing exceedingly well, others are just getting by and still others are losing money and will soon disappear from the marketplace. It is colourful and exciting and everyone is plying their trade to the best of their ability. This is how the marketplace works and it is easily understood on a small scale. Now magnify this small marketplace by ten million times or so, add hundreds of thousands of variables, and so many unaccounted for circumstances that you can't even begin to fathom its size and complexity. This is a rough approximation of the marketplace in which the fund manager and his team operates on a daily basis. It is so rich, diverse and unknowable that it defies description. So, now understanding the operating environment of financial markets, how does our fund manager, Chris Meyer, and his team, make investment decisions?

As a starting point to the investment process, the investment team considers the prevailing South African and global economic data. Based on this they use their experience to identify future trends that they believe may influence the direction of the overall economy and, within that, determine price movements of market segments (e.g. banking, mining etc.). Chris would then identify industries and asset classes that he would like to avoid for the next 12 to 36 months, as well as attempt to identify asset classes that he believes would outperform the available options.

As a next step, the identified suitable investments are placed on a watch list for a period of time. These investments are then monitored in terms of daily price and volume trends. Only after a period of 'observation' would consideration be given to possibly invest in any of these particular investment options. The general investment principals followed by us are listed as follows:

- With every investment there is a stop-loss in place. This means that should any of our selected investments fall by more than a certain percentage, we would close that investment position immediately.
- We prefer investments that provide an annuity income, and which have growing annuity income potential.
- We would look for companies with strong established brands, that also have strong balance sheets with limited intangible assets, a strong cash generating ability and that are not reliant on external factors to establish their products' selling prices (i.e. commodities).
- We are extra careful when investing in new technology, processes or ideas.
- We are not day traders.
- We acknowledge the principal that 'all' information is already known and discounted into the market and will never trade on a single source's recommendation.
- We diversify the portfolios to limit risk, but not excessively, as this would have the effect of destroying any possible *Alpha* (*active return on an investment*).
- We sell losers and keep winners, i.e. we will not 'hope' for a turn-around and we will not 'take profit' on winners while they are still having a positive momentum.
- We measure our portfolio performance against portfolios managed by other respected asset managers.
- We acknowledge mistakes.

## 2. News and performance of our two biggest funds

### IFM Technical Fund (Information sourced from Profile Media website (www.fundsdata.co.za)

The portfolio continue to steer clear of general resources as the fund manager believes that the uncertainties in future demand for commodities (such as iron, gold, etc.) will continue to place a negative sentiment on the companies in this sector. Cash holdings were further reduced during March 2016 by investing in local equities.

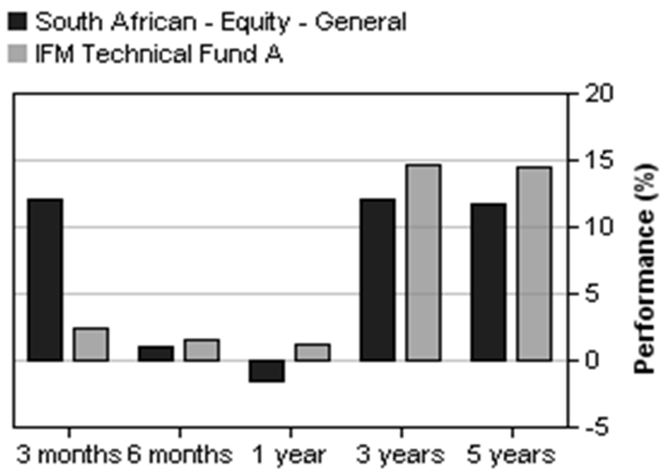
The portfolio aims to stay fully invested in equities with an over-exposure to Rand hedge equities. We believe that the Rand continues to be under pressure in the medium to long term although short-term strengthening can be expected. The portfolio is currently 48% invested in the following five securities, SAB Miller, Indequity Group Limited, British American Tobacco, Steinhoff International Holdings and Reinet Investments.

Investment in this specific fund has grown, for example, as follows:

- If you invested R1000 on 31 March 2015, it would have grown to be worth R1,045.71 on 31 March 2016 (4.57% annual compound return).
- If you invested R100 per month since 31 March 2015, the investment was worth R1,238.22 on 31 March 2016 (5.78% annual return compound monthly).

It is important that you try to not redeem money from your account as the growth of the portfolio, year-on-year, will then be significantly better.  Investments in unit trusts are long-term in nature and you could, in fact, lose money between the monthly debit order and when you make a redemption, because of short-term market movements.

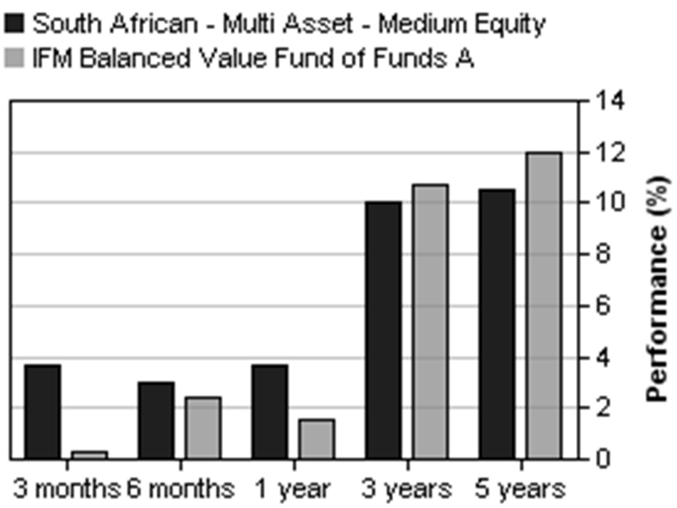
The graph below indicates its performance against the benchmark, over the last five year period:



**IFM Balanced Value Fund of Funds (Information sourced from Profile Media website (www.fundsdata.co.za)**

The IFM Balanced Value Fund of Funds is a well balanced fund that continues to be heavily invested in equities irrespective of the volatility that is seen in the equity markets currently. The portfolio will provide stable growth over the long-term. In the short-term we will always (as with any investment, apart from a bank deposit) have the possibility that growth will be low or even negative. In the long run you will however always beat inflation with this investment. In South Africa, with our weak currency and lots of imported goods, we will always have high annual inflation rates that we must try to protect our investments from.

96% of the fund is invested currently in the IFM Technical Fund, the Allan Gray Money Market Fund and Foord's Global Equity Feeder Fund. The fund manager is looking to increase the fund's international exposure in the coming months.




For most investors, the single most important thing when choosing between unit trusts is past performance. The funds that have generated the highest returns are the ones that attract the most attention. However, one has to consider the following two scenarios with this approach.

Firstly, many investors don't review the track record of performance over a long enough period, say 5 years. The returns over one year may look good, but it begs to ask the question whether the fund manager has demonstrated the ability to generate superior performance over a sustained period of time and through different market cycles?

Secondly, it is important to consider the risk that was taken to generate the return. This is particularly true over shorter time frames, where some risky positions may pay off handsomely. However, will the manager be able to protect those gains in the long run?

Both these portfolios (IFM Technical Fund and the IFM Balanced Value Fund of Funds) have done well in consistently outperforming the benchmarks, placing them in the top quartile of their categories.

- **Investment Returns for last 5 years**

  (Periods greater than one year are annualised and the fund's investment returns are shown after taking into consideration all costs and fees paid)(**Source: Morningstar**)

| | LAST 12 MONTHS | LAST 3 YEARS | LAST 5 YEARS | | LAST 12 MONTHS | LAST 3 YEARS | LAST 5 YEARS |
|---|---|---|---|---|---|---|---|
| **IFM Balanced Value FoF** | 5.27% | 11.12% | 12.40% | **IFM Technical Fund** | 5.37% | 14.84% | 15.00% |
| **Benchmark** | 0.25% | 8.43% | 10.55% | **Benchmark** | 1.66% | 12.30% | 13.15% |

## 3. Should I have exposure to an international investment portfolio?

For many investors, a real concern is the possibility of further Rand weakness given the current state of the local economy and the chance of a downgrade of South Africa's sovereign debt to 'junk' status. A question that is often asked is whether one should have a greater exposure to offshore markets.

As a general recommendation, one can say that every investor should be diversified into offshore markets. What differentiates each investor from the next is the consideration of the percentage of their assets that they should invest offshore. This is strongly determined by where each person is in his or her life, their current exposure to offshore and local markets, and the risk profile they are prepared to accept on their investment portfolio. Generally speaking, the higher your required return and the more risk you are prepared to take, the greater your offshore exposure should be.

If you invest in a multi-asset fund that is an underlying investment in a retirement fund or a retirement annuity fund, the fund's offshore exposure is limited to 25 percent of the portfolio in terms of the prudential investment guidelines contained in regulation 28 of the Pension Funds Act. Many shares on the JSE earn a sizeable portion of their earnings or profits from offshore markets and are therefore commonly referred to as rand-hedge shares. As a result, most people in a South African multi-asset fund that complies with regulation 28 have sufficient offshore exposure despite the 25-percent limit on offshore assets. You can invest in a rand-denominated fund that, in turn, invests in foreign markets, or you can invest directly in a fund domiciled offshore and denominated in a foreign currency. However, a rand-denominated fund saves you from complying with exchange control regulations and converting your money into a foreign currency via an offshore bank account.

If you do invest offshore, you should invest in equities, rather than cash or bonds. For cash, remember that real (after-inflation) interest rates are negative in the 19 countries that fall under the European Central Bank and in Japan, Switzerland and Denmark. Economic growth and inflation in these countries is likely to remain low, so interest rates will also be low. Bonds in many foreign countries are also offering very low returns. Accordingly, yields on short-dated bonds with a maturity of between 1 and 5 years are largely negative. Yields on 10-year bonds in Europe are about 0.2 percent, 1.7 percent in the United States and zero in Japan. Equities are, therefore, the preferred asset class for international exposure, because in almost all markets the dividend yields on equities, as represented by major indices, are typically above those on cash and bonds.

Both the IFM Balanced Value Fund of Funds and the IFM Technical Fund have an international exposure currently. In addition, we hope to finalise the establishment of a new international fund, which will be called "The Heiden Grimaud Global Fund (Euro)" which fund will invest directly in offshore equities. Chris is finalizing the last operational procedures and we hope to have the fund ready for marketing within the next two months. All our investors will be notified of the launch, should you be interested in a possible investment in this new investment option.