



FG INVESTMENT PARTNERS

GLOBAL BRIEF

Quarter 2 | 2023



EDITORIAL COMMENT

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Positive returns from global equities, but poor performance in other assets and domestic market

Another quarter has come and gone. South African investors with significant global developed market equity exposure would have been pleasantly surprised with a very positive return over the period. This area of the market combined with a weak rand to give returns of some 13% (MSCI World Index) in rand terms in just three months. This however would have been the only asset class area to elicit such satisfaction. Even within the developed market equity space, the bulk of the performance came from just eight Mega Cap Tech and Artificial intelligence stocks. As for the rest, there was little to get excited about and most other asset classes did not even come close over the quarter. Global bonds were negative in US dollar terms as interest rates continued to edge up and inflation deceleration proved to be quite slow. On the domestic front, investment returns were poor over the quarter with investors facing a poor economic outlook and a high interest rate environment. The uncertain political and international policy dynamic also contributed meaningfully to the rand's weakness. The FTSE/JSE All Share Index returned less than 1% and the FTSE/JSE All Bond Index returned a negative 1.5% over the same period. The money market proved to be the best local asset class at a return of just 1.3%.

Questions remain about inflation, interest rates, equities, corporate margins and the Chinese economy

Of course, this is all water under the bridge now. Still, uncertainties remain. While the US economy has proved surprisingly resilient (so far) in the face of a much higher interest rate environment and consumers have yet to tighten their belts, leading indicators continue to point to a slowdown further down the line. The following key questions are still plaguing investors' minds. Will the pace of inflation deceleration prove to be too slow (wage inflation is showing few signs of abating in a still relatively tight labour market) and in turn, result in further rate hikes from developed market central banks?

INDEPENDENT TRANSPARENT COMPETENT

Will the higher interest rate environment start to see increased savings and slower spending? Can global developed market equities keep up the momentum? Will corporate margins start to come under some pressure as economies slow? Will a sluggish Chinese economy start to respond more positively to stimulus measures?

Making predictions is notoriously difficult but while these questions persist, a cautious approach to risk and a good spread of assets (some at very attractive yields) fully makes sense to us. We continue to remain well diversified from an asset manager and style perspective.

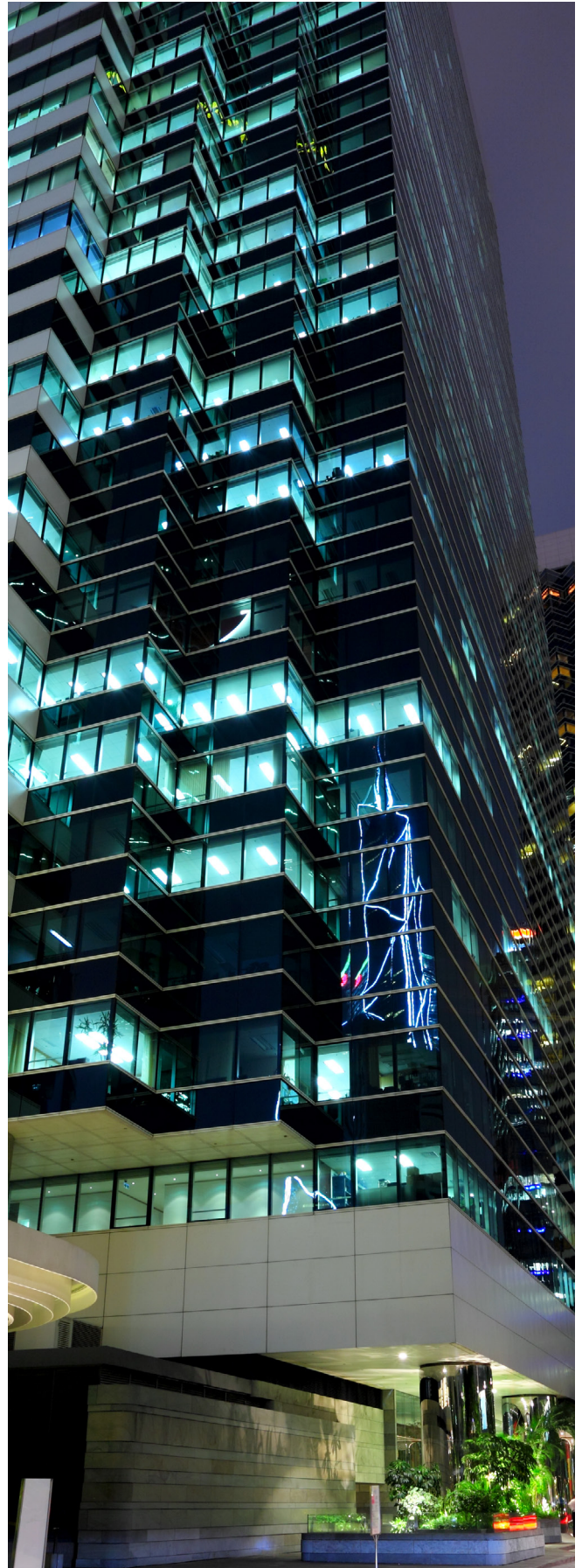
What you can look forward to in this edition

Renier de Bruyn, Head of Asset Allocation at Sanlam Private Wealth, speaks to the fragility of the rand and its bounce-back potential. This is particularly relevant given the latest bout of weakness in the local currency. Luzuko Nomjana, Prescient Portfolio Manager and Credit Structuring Specialist, considers the hurdles faced in plugging the electricity gap. He points out that with the private sector playing an increasingly important role: capital should not be a problem. Clyde Rossouw, Co-Head of Quality at Ninety One, talks about the end of the 'free-money' era and its implications for the health of corporate earnings. And finally, Anton Pillay, the CEO of Coronation Fund Managers, writes about 10 themes to guide the youth as they enter the workforce. Pillay focuses on the critical skills required to excel despite South Africa's alarming youth unemployment rate, the prevailing environment of economic uncertainty and the likely impact of artificial intelligence on the future of work.

We hope that you enjoy these articles.

As always, stay safe.

The FG Asset Management Investment Team



OUR FRAGILE CURRENCY: CAN THE RAND BOUNCE BACK?



Adapted from an article by
Renier De Bruyn

Head of Asset Allocation
Sanlam Private Wealth

A deeper look into the factors causing the rand to weaken

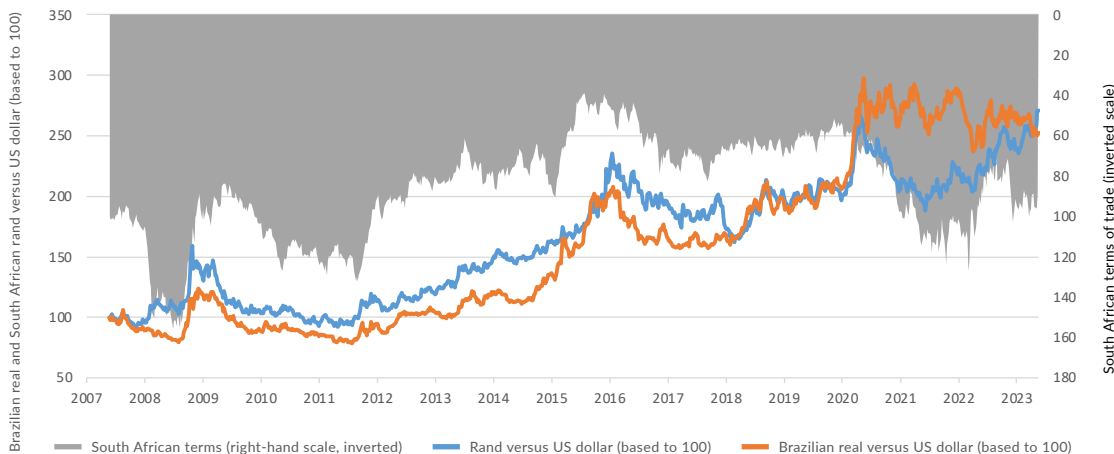
The rand has weakened severely over the past two years, losing more than 40% of its value against the US dollar since June 2021 – at the end of May this year, our beleaguered currency plunged to a new record low. Historically, the rand has always managed to recover from points of extreme pessimism, but with so much risk currently associated with South Africa, can we realistically expect this pattern to repeat? How does this impact long-term investment decisions?

Media commentators tend to attribute the movement of the rand to the political headlines of the day, but it's important

to distinguish between external global macroeconomic drivers and South Africa-specific factors when assessing our fragile currency's performance.

A simple way to determine whether external or internal factors are at play is by comparing the rand's movement to comparable emerging market currencies such as the Brazilian real, as seen in figure 1 below. We can also compare it to South Africa's terms of trade (a measure that shows the movement in the relative prices of our country's imports and exports, which correlate strongly with mining commodity prices).

Figure 1: South African rand versus Brazilian real and the terms of trade



Source: Bloomberg, SPW research

We can see here how important commodity prices are for the currencies of countries such as South Africa and Brazil. Both currencies are also impacted by global risk events, such as the global financial crisis in 2008 and 2009, and the COVID-19 pandemic in 2020 when emerging market currencies were generally shunned in favour of perceived safe havens such as the US dollar.

When these two currencies start to diverge, however, it's usually a sign that domestic factors have come into play. For example, the "Ramaphoria rally" in early 2018 resulted in abnormal rand strength, while Brazil clearly missed out on some of the post-pandemic recovery due to internal political issues. More recently, as loadshedding has intensified in South Africa since late 2022, the rand has noticeably started to underperform both its emerging market peers and the US dollar.

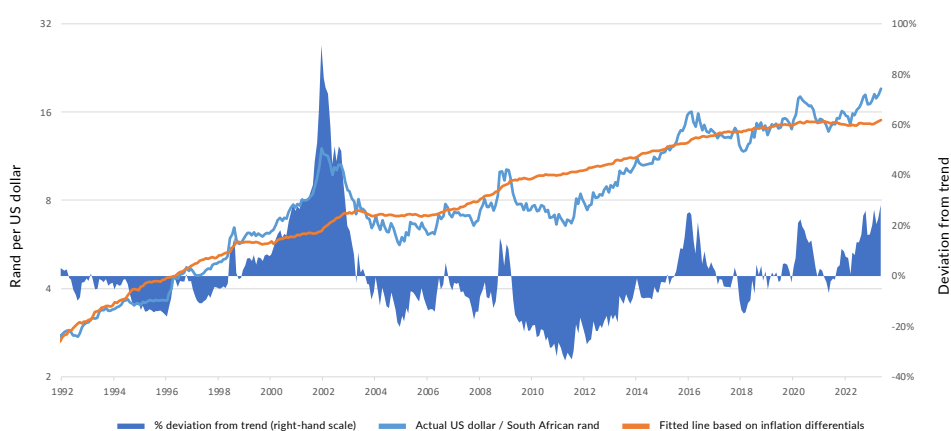
South Africa can only blame itself for its recent currency woes

The negative impact of severe loadshedding on economic growth and investor confidence is the direct result of the long-term mismanagement of the state-owned power utility. South Africa's grey listing by the Financial Action Task Force in February, and the public relations fallout resulting from our perceived association with Russia, are also self-inflicted wounds.

Historically, the rand has always managed to recover from points of extreme pessimism. However, given the number and extent of South Africa's "own goals", is it realistic to expect that the pattern will repeat?

The "fair value" of a currency is ultimately determined by its relative purchasing power. Figure 2 below shows a regression of the change in purchasing power (i.e., inflation differentials) versus the prevailing rand/US dollar exchange rate over the past 30 years. This has in the past been a useful indicator of the long-term fair value of the currency.

Figure 2: Fair value of the rand based on inflation differentials



Source: Bloomberg, SPW research

As can be seen on the figure above, the fair value of the rand is currently around R15/US dollar, with the current deviation (i.e., cheapness) of the rand in line with the extremes of the COVID-19 and Nenegate sell-offs. If the South African Reserve Bank (SARB) can continue to act independently in its mandate to anchor inflation within the 3-6% target range, there is a fair chance for the rand to return to fair value in time.

The value of the rand is dependent on improvements in other factors

The currency can deviate from this fair value for sustained periods, primarily driven by three factors:

1. Global risk sentiment (external factor).
2. Terms of trade (external factor).
3. Country-specific factors that impact its expected economic growth (domestic factors).

To move the rand back to fair value, we'll need to see an improvement in a combination of these three factors, while the SARB remains in control of its inflation mandate. While the valuation of the rand is undoubtedly cheap and the SARB has maintained its credibility, we're concerned that the global economic environment may not be supportive of the currency over the next year should the tight financial conditions result in a global recession.

Furthermore, the domestic ("self-help") factors depend heavily on an improvement in our electricity supply, and while investment in private generation should start alleviating some of the pressure in the future, the near-term outlook in terms of loadshedding remains worrisome. The national elections next year are further increasing investor uncertainty – the prospect of a coalition government that can take on a number of permutations with widely differing economic policy makes it difficult to take any bold views on the currency with confidence.

Another factor to consider is the higher offshore allowance for South African retirement funds (currently 45% versus 30% before 2022). Many pension fund managers were forced to repatriate funds during past spells of rand weakness so as not to breach the 30% offshore limit. This provided a natural countercyclical force for the currency. However, it seems as if most pension fund managers are currently still well below the revised 45% offshore limit, creating less impetus to start reversing the flow of money as was the case in previous cycles.

Is the pessimism priced in?

The recent market movements have resulted in attractive relative valuations for South African equities, bonds and the currency. In other words, there is already a great deal of pessimism priced into these assets. It would therefore be inappropriate to let fear drive indiscriminate selling of South African assets to buy foreign assets at these levels. Investors who did so in the 2001 cycle destroyed much material wealth over the following decade. We do, however, remain mindful of the structural challenges our economy faces. We'll therefore continue to advocate for globally well-diversified portfolios, but guard against pro-cyclical portfolio changes driven by fear or greed.

GRID AND BATTERY STORAGE CAPACITY, NOT CAPITAL, ARE HURDLES TO PLUGGING THE ELECTRICITY GAP



Adapted from an article by
Luzuko Nomjana

Portfolio Manager and
Credit Structuring Specialist
Prescient Investment
Management



Resolving South Africa's energy crisis hinges largely on two crucial elements:

1. Expanding the grid capacity.
2. Installation of sufficient battery storage capabilities.

When complemented with storage capacity, we are confident that renewable energy will go a long way in alleviating our energy woes.

Can renewable energy solve South Africa's power crisis?

Given South Africa's fiscal position, private participation in the rollout of infrastructure is essential to achieve the country's growth ambitions. Pursuantly, private capital remains available – private sector capital continues to be available when bankable investments, not only in renewable energy but across the breadth of the infrastructure ecosystem, are available. A case in point is the how competitive the last two Renewable Energy Independent Producer Procurement Programme (REIPPP) Bid Windows were, from a participation (i.e., volume of bids received) and from a returns perspective (i.e., lower tariffs).

However, Bid Window 6 (BW6) revealed the core challenge government and the private sector are faced with in increasing electricity generation by the required 78 gigawatt outlined in the Government's Integrated Resource Plan (IRP). Despite Eskom, being unable to meet the country's power demands, the lack of grid capacity means that the increasing output from renewable energy will ultimately be stranded.

Let's take a deeper look into the problems with the grid

It's well known that the Northern Cape no longer has any available grid capacity. However, in the recently awarded BW6, it became evident that neither do the Eastern and Western Cape corridors, popular for their abundant wind resource. The result was the curtailment to the initially envisaged BW6 capacity.

In response to increasing frequency of loadshedding, the government initially doubled the capacity available for tender from 2 600 megawatt (MW) in Bid 5 200MW in Bid Window 6 without having undertaken the necessary study of available grid capacity. The Bid Window was two times oversubscribed, yet only 1 000 MW was ultimately awarded, and not a single wind project was awarded due to the unavailability of grid capacity in the Eastern and Western Cape. Most of the Eastern and Western Cape grid capacity available when the bid window was released had subsequently been taken up by private generators when the bid was allocated. As noted by South African Wind Energy

Association, an independent assessment of the grid would be crucial in assessing solutions to this problem. We are supportive of the view that urgent attention is required to improve or unlock grid capacity.

Importantly, not addressing grid constraints, and consequentially the reduction in renewable energy as contribution to our energy mix would be a disaster for South Africa – if one considers that without the 6.2GW (6.5% of the total energy mix) provided by renewable energy sources in 2022, the country would've experienced more severe loadshedding. So, to the extent that renewable energy, as the cheapest and cleanest energy source, contributes towards an improving energy availability factor, it has an undeniably significant role to play as part of our energy mix.

Renewable energy is only a solution with effective storage capacity

To make the progress needed, we must be very clear on how far renewable energy can go in resolving our long-standing and frustrating energy challenges as a country.

In this context, it is important to understand energy generation on two levels – base load and peak load. Base load refers to a power source that can generate and deploy across a set of 24 hours, and peak load refers to the power that can meet spikes in demand over shorter periods.

Renewable energy, as procured through the country's REIPPP programme thus far, is inclement in nature. A wind farm can only generate electricity when the wind blows, and a solar photovoltaics (PV) farm can only generate power when there is sufficient Direct Normal Irradiation (DNI), the amount of solar radiation received per unit area.

Thus, to the extent that we need base load energy, renewable energy without storage capacity would not be sufficient. Efficient and cost-effective storage capacity is therefore crucial to store and dispatch the energy generated by renewables.

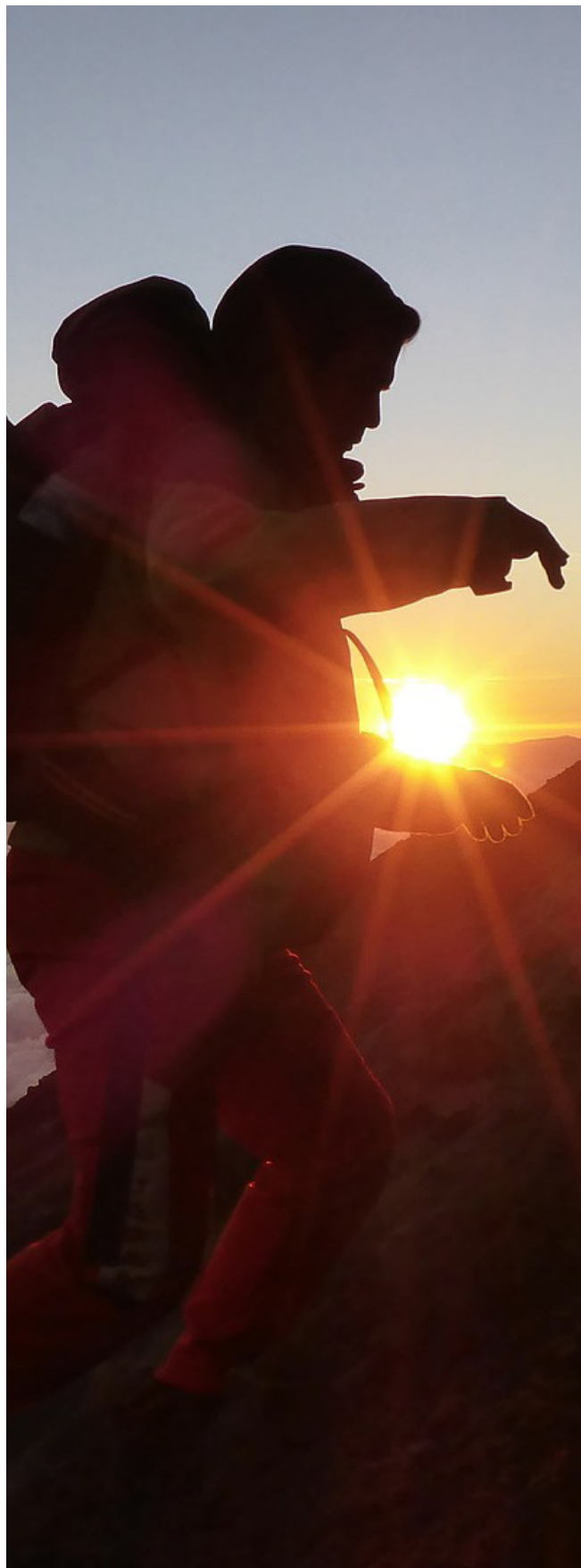
South Africa has come a long way in a short period of time

This is one of the key reasons the Independent Power Producer (IPP) Office has released a request for proposal to procure battery energy storage technology (513MW through the first phase), which, when complemented with solar or wind generation, will provide clean base-load energy. All five of these prospective battery storage sites are situated in the Northern Cape province. This is where most of the country's solar plants are located, with the intention that these projects provide capacity, energy and ancillary services to Eskom. Further signs of progress the government has made in the transition to renewables include streamlining the process to ensure the swift implementation of renewable alternatives. This bid submission is scheduled to close on July 5, 2023.

Although a lot still needs to be done, we've come a long way in a relatively short period of time. Not too long ago, no one was allowed any private generation plant above 1MW. The Energy Action Plan however, recently announced the removal of licensing requirements (they still need to be registered) for generation projects of any size to enable private investment at a much larger scale.

Environmental and land-use authorisation timelines have also been reduced across the board. Thus, it's evident that government is making a concerted effort to create an ecosystem that fast-tracks the addition of new, low-carbon generation capacity, and the necessary conditions are being put in place to fast-track investment in renewables in South Africa.

Renewable energy enjoys policy support and political willingness, two critical tenets necessary for long-term investment decision making. The recent release of the Energy Action Plan is further evidence of this. Thus, if we have this clear policy certainty and a live/regularly updated Integrated Resource Plan that we adhere to, we'll continue to enjoy sufficient availability of private capital to unlock South Africa's abundant supply of wind and solar resources.



BACK TO INVESTMENT BASICS AS 'FREE-MONEY' ERA ENDS



Adapted from an article by
Clyde Rossouw

Co-Head of Quality
Ninety One



Key takeaways

- Post the Global Financial Crisis, we experienced an era of cheap money, which distorted the cost of capital and favoured excessive risk-taking.
- The return of persistent inflation has forced central banks to hike interest rates aggressively, bringing an end to 'free money'.
- Many businesses had positioned themselves for a low-rate environment and now that the tide has turned, some are ill-prepared for higher rates.
- Despite tough conditions, high-quality businesses with exceptional fundamentals should come into their own.

The rise of excessive risk-taking over the past decade and a half

When I started my career in the investment markets in 1995, high positive real interest rates were the norm. That all changed when the Global Financial Crisis hit during 2008, ushering in the era of easy money. For the next decade and a half, markets operated within a false equilibrium, where near zero or negative interest rates and quantitative easing distorted the cost of capital, which in turn encouraged excessive risk-taking. When economies and markets tanked during the pandemic, policy makers provided massive stimulus measures to help alleviate tough financial conditions. But persistent inflation has brought an end to the 'new normal', as central banks across the world have been forced to hike interest rates aggressively to restore price stability.

During restrictive financial conditions, financial 'accidents' are more likely to occur. Many businesses had positioned themselves for a low-rate environment and now that the tide has turned, some are ill-prepared for higher rates. Non-profitable technology companies have come under pressure. We have also witnessed turmoil in the global banking sector, with the collapse of Silicon Valley Bank, Signature Bank, and the bailout of Credit Suisse.

The US Federal Reserve (Fed) is sticking to its guns

Despite these developments, the Fed is committed to raising rates to lower inflation. It has been able to stick to its guns by making additional funding available to financial institutions to prevent banking liquidity or solvency issues.

Rising interest rates have been a major headwind for markets. Investors continue to focus strongly on when the US will reach the point at which inflation and the Fed's funds rate will converge. While global inflation has been a real worry, the health of corporate earnings deserves closer scrutiny.

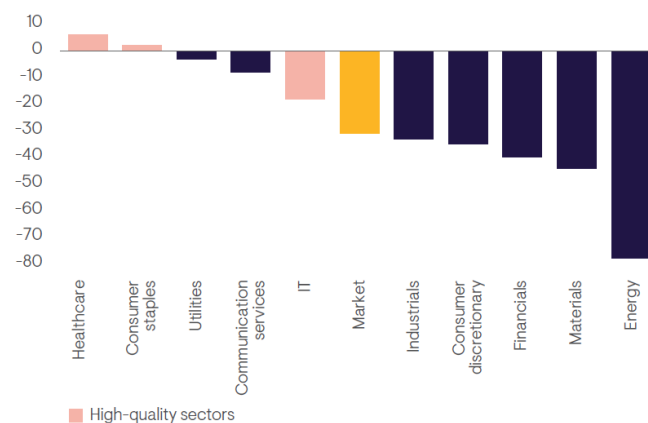
A gloomy economic outlook

Manufacturing activity has been contracting sharply in the US, reflecting the gloomy economic outlook. The bond market is also signalling that it is expecting a significant downturn in economic activity this year, as evidenced by long-term rates being much lower than short-term rates. The difference between 10-year rates and three-month rates is the steepest it's been since 1981.

Cyclical businesses are feeling the pressure. As companies start losing volumes, their pricing power will suffer – impacting their earnings growth. While a recovery in economic growth in China could provide some relief, it is going to be a tough year for company earnings.

How deep is the earnings trench?

Average global sector earnings percentage change during previous earnings recessions.



Source: Citi Research, Global Equity Strategy, October 2022, Market: MSCI ACWI.
Global EPS recession dates: 31 Jan 2008 – 29 Jan 2010; 27 Feb 2015 – 31 Oct 2016;
31 Mar 2020 – 30 Nov 2020.



The figure above shows that during difficult market conditions the energy, financials, materials and consumer discretionary sectors typically experience a far greater hit to profits compared to other parts of the market. It's not to say the energy sector will experience such violent moves. High-quality healthcare and consumer staples earnings are more resilient during economic downturns. But these sectors generally have lower levels of growth, so investing in other high-quality opportunities that offer long-term growth is key.

Semiconductors – attractive structural growth trends

Semiconductors, also known as chips, are the brains of all modern electronics. We find them in smartphones, tablets, computers, data centres, autos and more. Semiconductors have attractive structural growth trends, with some predicting the industry will top US\$1 trillion by 2030. But because of inherent cyclical risks, it is important to seek out companies with sound business fundamentals and compelling long-term growth prospects.

Advanced Semiconductor Materials Lithography (ASML) is a key portfolio holding

ASML focuses on the lithography step of the chip-making process, which is almost like a high-tech photocopier. Its extreme ultraviolet light (EUV) machines which are approximately the size of a single-decker bus, cost US\$150 million, and have become precisely what chip makers need to print smaller circuits while increasing capacity and speed. In the EUV era, ASML is no longer just a dominant supplier, but rather a monopoly, created through technological brilliance and innovation, as opposed to the more traditional mergers and acquisitions route.

Taiwan Semiconductor Manufacturing Company (TSMC) is another portfolio holding in this growth sector

It is the world's largest contract manufacturer of chips. The company posted strong financial earnings earlier this year. Even though the chip industry is experiencing a cyclical downturn, TSMC still expects some growth in 2023. Its long-term growth profile remains firmly intact. Against a backdrop of difficult financial conditions, TSMC maintains a strong financial position, and has excellent credit ratings, as well as a healthy balance sheet. TSMC has not needed external funding to finance organic growth.

Experiences making a strong comeback

Coming out of the pandemic, the growth in the leisure sector has been robust, reflecting people's pent-up demand for holidays. Consumers are choosing again to invest money in experiences over goods, which has benefited the leisure industry across the board. This year, we are also seeing a recovery in Asia's travel industry, particularly from China, after lifting COVID-19 restrictions. The devastating impact of the pandemic wiped out many players in the hospitality industry, so it's not quite 'business as usual' yet. Although the industry still has its challenges, there are good valuations and growth on offer for discerning investors despite recent gains.

Booking Holdings, an industry-leader in online travel

The company is well positioned to capitalise on the recovery in the leisure sector, and it has provided an upbeat forecast for the year. Room nights booked in January were 26% – higher than 2019 levels. The online giant is expecting percentage growth for gross bookings in the low teens compared to the 2022 levels. Booking Holdings is well positioned to capitalise on the recovery in the leisure sector.

In conclusion

Now that the 'free-money' era has ended, it's time to dust off the old investment playbook and revisit the old-fashioned principles of investing. We are going back to a world where fundamentals matter. Valuation and energy were last year's theme, but we don't believe they will drive the stock market performance this year. The problem with businesses that are merely cheap is that their valuation does not protect you when the fundamentals change for the worse. Cheap shares can be very risky in a difficult market environment. We expect balance sheets and earnings to take centre stage this year.

Geopolitical uncertainty will prevail, but inflation is likely to moderate as demand cools and companies and individuals repay their debt. Despite tough conditions, there is money to be made – high-quality businesses with exceptional fundamentals should come into their own.

10 THEMES TO GUIDE THE YOUTH AS THEY ENTER THE WORKFORCE



Adapted from a Youth Day interactive session with Anton Pillay

CEO of Coronation and Chairperson of ASISA Coronation

Every year, at the start of Youth Month in June, Coronation CEO Anton Pillay spends quality time with learners to share valuable life and career advice ahead of their journeys into adulthood and the world of work. This year, Pillay visited the Grade 10 and 11 learners from Christel House (educational non-governmental organisation) in Ottery and, later, hosted students from various university investment societies who are interested in pursuing careers in business and finance.

In these sessions, he focused on the critical skills required to excel, despite South Africa's high youth unemployment rate, the prevailing environment of economic uncertainty and the likely impact of artificial intelligence (AI) on the future of work.

Ten key themes the youth should consider before joining the workforce:

1. If you are privileged with an education, use it for good and you will find your purpose

In a country where 78% of Grade four learners cannot read for meaning and where the youth unemployment rate is more than 60%, you are in a fortunate position to complete matric with a solid education. A university degree offers you a higher chance of employment, but it is no guarantee of success. You need to think smart, not only about what you want to achieve in your own life but also how you can contribute to the betterment of society. If you can focus on excelling with the opportunities you were given, you will find your purpose and live a more fulfilled life.

2. Use of technology to the benefit of your career and society

Technology advances such as big data and AI undergoing an exponential evolution at the moment, and in the careers of tomorrow, it will be important to have a grasp of these technologies. It is safe to say that graduates should be upskilled to use AI in their roles. It is also important to distinguish how good actors and bad actors are able to use AI differently, and to make a commitment to, one day in your career if you are going to use AI, use AI ethically and responsibly in line with the 'Principles for the Ethical Use of Artificial Intelligence in the United Nations System'. However, it is a very complex topic that is set to disrupt many industries. The aim should be to enhance efficiencies and boost performance alongside human capital.

It is safe to say that graduates should be upskilled to use AI in their chosen careers. While much has been written about AI displacing people, the financial services arena is all about talent, diversity, culture, and talent recruitment and retention, which will always be a core differentiator.

3. Hone your critical thinking

The World Economic Forum reports that critical thinking is the top scarce skill of this decade. Critical thinking is the ability to use reason and logic to analyse and assess situations and problems to make informed decisions. Don't just take everything at face value or believe what you are told. Learn to think and solve problems for yourself. The key principle here is probability – you must critically assess how probable any supposed 'fact' might be and find real evidence to support it, instead of relying on opinions, gossip or conspiracy theories.

4. Embrace creative thinking

Embracing your creativity does not necessarily mean artistic creativity. One can also use creative thinking to solve hard problems in business and society. Creativity is the foundation of innovation and to developing something new. It's the ability to find new solutions to existing issues. The key is to always look for possibility in every challenging situation.

5. Remember, collaboration is at the heart of any economic endeavour

Sometimes you have to put in the hard yards on your own, it can be tough, and self-motivation and self-management are key. However, please remember, you don't always have to do it on your own, all of the time. Teamwork, collaboration and being open to diverse viewpoints are essential for achieving success in business.

6. Learn to communicate clearly

Less is more. Regardless of the career you ultimately pursue, you will discover that communicating clearly results in more successful outcomes. Every email you write, every presentation you deliver, every report you write, every difficult conversation you have with colleagues or managers, you will do better if you use less words, chosen wisely, and that are very clear in their meaning. As Winston Churchill famously said, "It takes more time and effort to be short and to the point, but it is always more effective". Also remember, there are verbal and nonverbal skills, and body language is also very important to master.

7. Be entrepreneurial

Entrepreneurial thinking is not just for people who start new businesses – it's for anyone in business. It's a mental attitude essential for navigating change and success. Always think abundantly in terms of the opportunities you can explore and create for yourself and others. The one thing you can do to empower yourself is to walk through every open door, work hard and participate in life and the opportunities it presents you. You never know who you are going to meet, or what is around the next corner. But if you are prepared through consistent hard work, you'll be ready to take advantage of the opportunities and field the curveballs that life presents you.

8. Expect curveballs

The world is in a state of 'permacrisis', where one crisis seems to roll into the next one and it's easy for young people to feel hard done by. Remember that all young generations in every century of history faced a multitude of crises. It's part of the human experience. It just feels more amplified now because we have the internet and social media. This is not something to feel defeated by. Remember, a crisis always brings opportunity. If you expect curveballs, make sure you have prepared well and remain flexible and optimistic, you will find your way.

9. Take good care of yourself

Don't expect others to do your self-care for you. This is something you must attend to yourself. Try to cultivate healthy habits from as early on as possible, including healthy eating, getting regular exercise, resting, alone time, community engagement, taking care of your mental health, and maintaining good hygiene (even digital hygiene). Start with the small things, such as keeping your room tidy and your clothes, hair and teeth clean – small positive habits will translate into bigger positive effects in your life over time. Take personal responsibility for your wellbeing.

10. Don't let the high unemployment rate daunt you

This is a time in your life where you get to set the scene and choose your direction. Your voice counts. Yes, South Africa's unemployment rate is very high, but remember you always have options. If you don't see options, you can create opportunities – if you can't find a job, start a business that solves a problem that you see in the world. Surround yourself with people who support you, who also lean into the future, and who challenge you to be the best you can be. Don't hang out with negative people who limit you, as they will keep you stuck.

It doesn't matter if you haven't figured out what you want from your life and career yet – the most important thing is lean into your opportunities, talents and skills that are needed out there. No one can rob you of your future if you are proactive and positive. Be the rising tide that lifts others up too.





FG ASSET MANAGEMENT

QUARTERLY REPORT

Quarter 2 | 2023

ARCHITECTS OF SENSIBLE INVESTMENT SOLUTIONS

MARKET COMMENTARY



Jacy Harington
Portfolio Manager
FG Asset Management

Global growth has been unexpectedly resilient regardless of elevated inflation

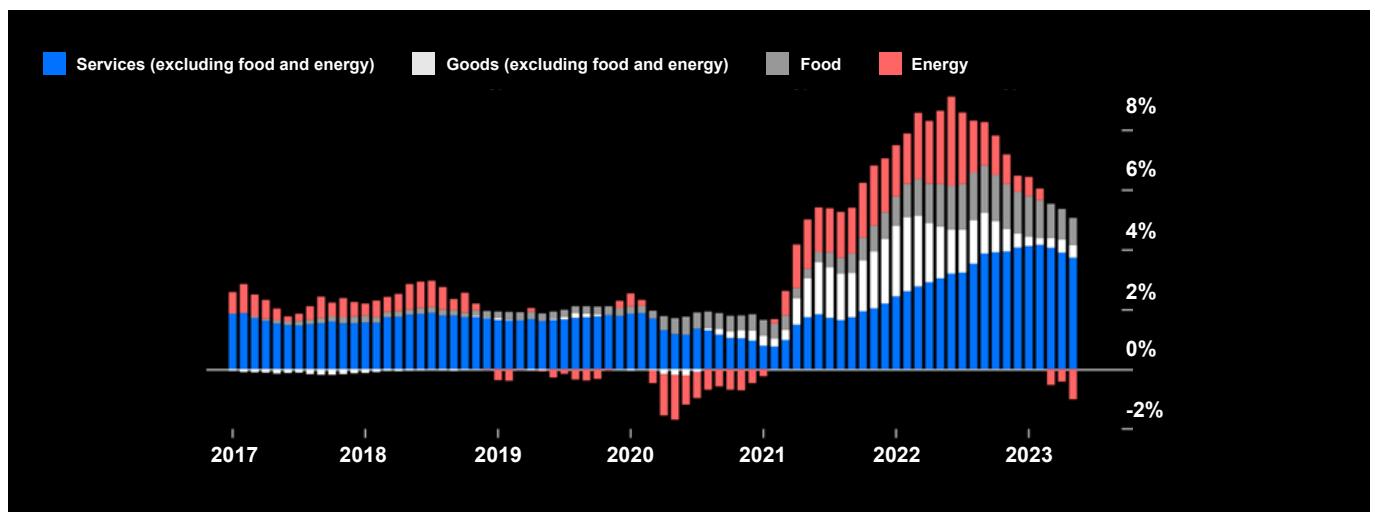
Over the past year, global central banks have delivered significant policy tightening with the aim to ease rising price pressures. Even though inflation has declined, it remains well above targets. This brings uncertainty around the duration and the extent of additional future restrictive monetary policy that will be required. This of course will have negative growth implications; however, the extent of the

global growth slowdown remains uncertain especially as growth has remained unexpectedly resilient until now. We have also witnessed some of the unintended consequences of the significant tightening come through in terms of further bank failures in the US. The market was content that the specific bank failures had been contained, but the risk of tighter credit standards remains a threat to economic growth. In addition, local asset valuations have come under pressure over the past three months given the worsening power crisis, poor growth outlook and the accusation of selling arms to Russia.

Inflation continues to influence the tightening of monetary policies

Inflation remained a significant market driver given its importance in determining the extent to which global central banks will need to tighten monetary policy further. US inflation has been coming down steadily over the past year, declining 5.1% from its peak in June last year at 9.1%. The problem remains however that even with the significant easing of price pressures, it still remains at 4%, double that of its 2% target. Elevated inflation is currently being propped up by shelter inflation, which if excluded brings headline inflation down to 2.1%. Shelter inflation tends to be backward looking as it includes rents of units of continuing renters and not just rents that are up for renewal. It usually takes between 12 to 18 months for shelter inflation to reflect current market conditions.

Figure 1: US inflation breakdown



Source: Bloomberg, (2017 to 2023)



Employment opportunities and wages continued to decline in the US

US employment data was also closely followed as it serves as a good gauge for the health of the economy and also provides insight into wage growth. The US labour market has been very robust as the unemployment rate has remained around historical low levels. The most recent release in June, however, did hint at some weakness as it increased to 3.7%. Wage growth has been falling too but like overall inflation at a much slower pace than anticipated.

The US Federal Reserve (Fed) held two meetings over the quarter, hiking rates by 0.25% at its May meeting to bring the Fed's funds range to 5-5.25%. The hikes that occurred in May were the central bank's 10th increase since it started hiking rates in March last year – increasing interest rates by 5% and bringing them to the highest level since before the global financial crisis in 2007. At the June meeting, the Fed left interest rates unchanged to provide room to assess the impact that the tighter monetary policy and credit conditions have had on inflation and economic growth. Fed Chairman, Jerome Powell, however, stressed that if inflation did not decidedly ease that interest rates would need to be raised further. It is also important to note that the Fed is not implying a reduction of rates into yearend but rather at least keeping interest rates at current levels, while they assess if the inflation is meaningfully moving towards the 2% target.

The extension of the US's debt ceiling brought about more uncertainty, which if not agreed upon would have created significant economic risks as the US government would have been unable to pay any of its financial obligations. Early June, however, saw relief in markets as a new bill was passed by the Senate that suspended the debt ceiling until January 2025.

The rand continued to depreciate in the second quarter

Locally the South African Reserve Bank (SARB) only held one meeting over the quarter, where they increased the repo rate by 0.5% to bring it to 8.25%, the highest level in 14 years. While the 0.50% rate hike at the May meeting was unanimous and widely expected, the statement following the announcement that the currency could likely weaken further "given upside inflation risks, larger domestic and external financing needs, and loadshedding" led to the rand depreciating significantly on the day. The Monetary Policy Committee (MPC) also see the current policy as restrictive which does give the indication that they see interest rates nearing their peak however later clarified that this does not keep them from moving policy more restrictive if required.

Local inflation remained high, despite the decrease in fuel prices and the slow rise in food prices

The rate increases came despite headline inflation rate falling overall from 7.1% to 6.3% over the quarter. The decline was predominantly driven by the easing of fuel prices, and encouragingly food price increases seem to be waning. Falling fuel prices are expected to help headline inflation return to the 3% to 6% inflation target range in the second half of this year, however inflation risks remain to the upside given the weak currency, excessive loadshedding and increasing administered prices all adding upward pressure to prices.

Local market concerns rose after South Africa was alleged to have provided weapons to Russia

In May, the allegations by the US ambassador that South Africa had secretly supplied arms and ammunition to Russia drove significant risk-off sentiment in local markets. Local assets saw a significant loss in value as the market started pricing in the consequences of possible sanctions or the removal of South Africa from the preferential trade agreement, African Growth and Opportunities Act (AGOA) with the US. The South African government denied the allegations and responded with an inquiry into the matter which did little to ease market concerns. This could be put down to other factors driving South Africa's risk premium higher such as the intensifying power crisis where the possibility of a grid collapse increased the compensation demanded by investors.



FG SCI* JUPITER INCOME FUND OF FUNDS

For periods until 30 June 2023

Performance and quartile ranking in sector | Launch date 15 August 2005

	Year to Date	6 Months	1 Year	3 Years*	5 Years*	10 Years*	Since Inception*
FG SCI Jupiter Income FoF	3.73%	3.73%	8.07%	6.59%	6.74%	7.10%	7.67%
STeFI Composite Index	3.70%	3.70%	6.76%	4.98%	5.81%	6.26%	6.90%
ASISA SA Multi Asset Income Category Average	3.67%	3.67%	7.94%	6.64%	6.77%	6.90%	7.54%
				1 st Quartile	2 nd Quartile	3 rd Quartile	4 th Quartile

*Data longer than 12 months are annualised

Source: Morningstar, performance for A class shares

Annualised returns are period returns re-scaled to a period of 1 year

Underlying funds

- Abax Flexible Income Fund (Nedgroup)
- Granate BCI Multi Income Fund
- Matrix SCI Stable Income Fund
- Prescient Income Provider Fund
- Terebinth SCI Strategic Income Fund (Amplify)

Performance statistics

	Fund	Benchmark
Highest 12-month performance	11.61%	11.77%
Lowest 12-month performance	3.25%	3.76%
% Positive months	92.99%	100.00%

*Source until 31 May 2018: MoneyMate

Source from 30 June 2018: Morningstar

The FG SCI Jupiter Income Fund of Funds returned +1.23% in the second quarter of 2023 and +8.07% over the past 12 months, underperforming the benchmark Alexander Forbes Short Term Fixed Income Index quarterly return of +1.92%, while outperforming the 12-month return of +6.76%. The Matrix SCI Stable Income Fund was the best-performing underlying fund over the quarter, returning +1.88%. No changes were made to the fund over the quarter.

Asset allocation as at 31 May 2023

	Local Equity	Local Property	Local Bonds	Local Cash	Foreign
FG SCI Jupiter Income FoF	0%	2%	47%	44%	7%



FG SCI* VENUS CAUTIOUS FUND OF FUNDS

For periods until 30 June 2023

Performance and quartile ranking in sector | Launch date 2 July 2007

	Year to Date	6 Months	1 Year	3 Years*	5 Years*	10 Years*	Since Inception*
FG SCI Venus Cautious FoF	6.37%	6.37%	12.38%	8.88%	7.83%	8.18%	8.55%
ASISA SA Multi Asset Low Equity Category Average	5.80%	5.80%	11.48%	8.38%	6.76%	7.03%	7.44%
				1 st Quartile	2 nd Quartile	3 rd Quartile	4 th Quartile

*Data longer than 12 months are annualised

Source: Morningstar, performance for A class shares

Annualised returns are period returns re-scaled to a period of 1 year

Underlying funds

- 36ONE BCI Equity Fund
- Abax Opportunity Fund (Nedgroup)
- Coronation Global Optimum Growth Feeder Fund
- Fairtree Equity Prescient Fund
- Granate BCI Multi Income Fund
- Matrix SCI Defensive Balanced Fund (Amplify)
- Matrix SCI Stable Income Fund
- Ninety One Diversified Income Fund
- Ninety One Global Multi-Asset Income Feeder Fund
- Ninety One Global Franchise Feeder Fund
- Prescient Income Provider Fund
- Saffron BCI Opportunity Income Fund
- Satrux Bond Index Fund
- Sanlam Multi Managed Inflation Linked Bond Fund
- Terebinth SCI Strategic Income Fund (Amplify)
- Veritas Global Equity Feeder Fund (Nedgroup)

Performance statistics

	Fund	Benchmark
Highest 12-month performance	16.83%	17.26%
Lowest 12-month performance	-1.41%	-3.15%
% positive months	71.88%	70.83%

*Source until 31 May 2018: MoneyMate

Source from 30 June 2018: Morningstar

The FG SCI Venus Cautious Fund of Funds returned +2.50% in the second quarter of 2023 and +12.38% over the past 12 months, outperforming the benchmark peer group average quarterly return of +2.14%, and the 12-month return of +11.48%. The Ninety One Global Franchise Feeder Fund was the best-performing underlying fund, returning +11.46% over the quarter. Over the quarter the fund's South African nominal bond and inflation linked bond exposure was reduced and rotated into shorter duration fixed income funds. In addition, the fund's global equity exposure was reduced, this was also switched into shorter duration fixed income funds.

Asset allocation as at 31 May 2023

	Local Equity	Local Property	Local Bonds	Local Cash	Foreign
FG SCI Venus Cautious FoF	13%	2%	29%	35%	21%



FG SCI* SATURN MODERATE FUND OF FUNDS

For periods until 30 June 2023

Performance and quartile ranking in sector | Launch date 15 August 2005

	Year to Date	6 Months	1 Year	3 Years*	5 Years*	10 Years*	Since Inception*
FG SCI Saturn Moderate FoF	7.16%	7.16%	14.12%	11.62%	8.43%	8.45%	10.06%
ASISA SA Multi Asset Medium Equity Category Average	6.66%	6.66%	13.37%	9.88%	7.19%	7.38%	8.73%
				1 st Quartile	2 nd Quartile	3 rd Quartile	4 th Quartile

*Data for longer than 12 months are annualised

Source: Morningstar, performance for A class shares

Annualised returns are period returns re-scaled to a period of 1 year

Underlying funds

- 36ONE BCI Flexible Opportunity Fund
- Abax Opportunity Fund (Nedgroup)
- Bateleur Flexible Prescient Fund
- Coronation Market Plus Fund
- Coronation Global Optimum Growth Feeder Fund
- Matrix SCI Defensive Balanced Fund (Amplify)
- Matrix SCI Stable Income Fund
- Ninety One Opportunity Fund
- PSG Flexible Fund
- Rezco Value Trend Fund
- Satrix Bond Index Fund
- Terebinth SCI Strategic Income (Amplify)
- Truffle SCI Wealth Protector Fund (Amplify)

Performance statistics

	Fund	Benchmark
Highest 12-month performance	31.40%	26.41%
Lowest 12-month performance	-18.22%	-15.68%
% positive months	69.63%	65.89%

*Source until 31 May 2018: MoneyMate

Source from 30 June 2018: Morningstar

The FG SCI Saturn Moderate Fund of Funds returned +2.69% over the second quarter of 2023 and +14.12% over the past 12 months, outperforming the benchmark peer group average quarterly return of +2.52%, and the 12-month return of +13.37%. The Coronation Global Optimum Growth Feeder Fund was the best-performing underlying fund, returning +8.06% over the quarter. As a result of the new allocation that was made to the Truffle SCI Wealth Protector Fund (Amplify), the Truffle SCI Flexible Fund's exposure needed to be prorated to the 36ONE BCI Flexible Opportunity Fund and the Bateleur Flexible Prescient Equity Fund in order to maintain diversification. Over the quarter the fund's South African nominal bond exposure was reduced and rotated into shorter duration fixed income funds. In addition, the fund's global equity exposure was reduced, this was also switched into shorter duration fixed income funds.

Asset allocation as at 31 May 2023

	Local Equity	Local Property	Local Bonds	Local Cash	Foreign
FG SCI Saturn Moderate FoF	28%	2%	25%	16%	29%



FG SCI* NEPTUNE GROWTH FUND OF FUNDS

For periods until 30 June 2023

Performance and quartile ranking in sector | Launch date 1 September 2014

	Year to Date	6 Months	1 Year	3 Years*	5 Years*	Since Inception*
FG SCI Neptune Growth FoF	6.84%	6.84%	14.68%	12.75%	8.89%	7.77%
ASISA SA Multi Asset High Equity Category Average	7.36%	7.36%	14.65%	11.41%	7.49%	6.55%
			1 st Quartile	2 nd Quartile	3 rd Quartile	4 th Quartile

*Data for longer than 12 months are annualised

Source: Morningstar, performance for A class shares

Annualised returns are period returns re-scaled to a period of 1 year

Underlying funds

- Coronation Global Optimum Growth Feeder Fund
- Fairtree Equity Prescient Fund
- Laurium Flexible Prescient Fund
- Matrix SCI Stable Income Fund
- M&G Balanced Fund
- Ninety One Equity Fund
- Ninety One Global Franchise Feeder Fund
- PSG Flexible Fund
- Rezco Value Trend Fund
- Saffron BCI Opportunity Income Fund
- Satrix Bond Index Fund
- Sanlam Multi Manged Inflation Linked Bond Fund
- Terebinth SCI Strategic Income (Amplify)
- Truffle SCI Flexible Fund
- Veritas Global Equity Feeder Fund (Nedgroup)

Performance statistics

	Fund	Benchmark
Highest 12-month performance	38.17%	30.65%
Lowest 12-month performance	-11.21%	-10.44%
% positive months	63.21%	62.26%

*Source until 31 May 2018: MoneyMate

Source from 30 June 2018: Morningstar

The FG SCI Neptune Growth Fund of Funds returned +2.64% over the second quarter of 2023 and +14.68% over the past 12 months, underperforming the benchmark peer group average quarterly return of +2.98%, while performing in line with the 12-month return of +14.65%. The Satrix Bond Index Fund was the worst-performing underlying fund, returning -1.61% over the quarter. Over the quarter the fund's South African nominal bond and inflation linked bond exposure was reduced and rotated into shorter duration fixed income funds. In addition, the growth asset exposure was reduced in the fund through rotating exposure from a combination of global equity, local equity and local property into shorter duration fixed income funds.

Asset allocation as at 31 May 2023

	Local Equity	Local Property	Local Bonds	Local Cash	Foreign
FG SCI Neptune Growth FoF	37%	2%	16%	11%	34%



FG SCI* MERCURY EQUITY FUND OF FUNDS

For periods until 30 June 2023

Performance and quartile ranking in sector | Launch date 15 August 2005

	Year to Date	6 Months	1 Year	3 Years*	5 Years*	10 Years*	Since Inception*
FG SCI Mercury Equity FoF	4.80%	4.80%	15.47%	16.66%	9.25%	8.79%	10.46%
FTSE/JSE Africa All Share (Total Return)	5.86%	5.86%	19.58%	16.12%	9.59%	10.32%	12.62%
ASISA SA Equity General Category Average	3.08%	3.08%	12.25%	14.28%	6.97%	7.43%	10.00%
				1 st Quartile	2 nd Quartile	3 rd Quartile	4 th Quartile

*Data longer than 12 months are annualised

Source: Morningstar, performance for A class shares

Annualised returns are period returns re-scaled to a period of 1 year

Underlying funds

- 36ONE BCI Equity Fund
- Coronation Global Optimum Growth Feeder Fund
- Fairtree Equity Prescient Fund
- Gryphon All Share Tracker Fund
- Laurium Equity Fund (Nedgroup)
- Ninety One Equity Fund
- Ninety One Global Franchise Feeder Fund
- M&G Equity Fund
- PSG Equity Fund
- Truffle SCI General Equity Fund

Performance statistics

	Fund	Benchmark
Highest 12-month performance	56.15%	53.98%
Lowest 12-month performance	-31.68%	-37.60%
% positive months	62.15%	61.21%

*Source until 31 May 2018: MoneyMate

Source from 30 June 2018: Morningstar

The FG SCI Mercury Equity Fund of Funds returned +1.22% in the second quarter of 2023 and +15.47% over the past 12 months, outperforming the +0.66% quarterly return of the benchmark FTSE/JSE All Share Total Return Index while underperforming the 12-month return of +19.58%. The Ninety One Global Franchise Feeder Fund was the best performing underlying fund, returning 11.46% over the quarter. No changes were made to the fund over the quarter.

Asset allocation as at 31 May 2023

	Local Equity	Local Property	Local Bonds	Local Cash	Foreign
FG SCI Mercury Equity FoF	74%	2%	0%	5%	19%



FG SCI* INTERNATIONAL FLEXIBLE FUND OF FUNDS

For periods until 30 June 2023

Performance and quartile ranking in sector | Launch date 17 October 2007

	Year to Date	6 Months	1 Year	3 Years*	5 Years*	10 Years*	Since Inception*
FG SCI International Flexible FoF	18.83%	18.83%	23.86%	7.13%	8.02%	9.95%	8.90%
Benchmark**	18.75%	18.75%	24.34%	7.58%	9.53%	10.45%	9.88%
ASISA Global Multi Asset Flexible Average***	18.75%	18.75%	24.34%	7.58%	9.53%	10.44%	8.97%
				1 st Quartile	2 nd Quartile	3 rd Quartile	4 th Quartile

*Data for longer than 12 months are annualised

Annualised returns are period returns re-scaled to a period of 1 year

**Benchmark before June 2013: 50% MSCI World Index, 50% JP Morgan Global Government Bond Index

Benchmark between July 2013 and July 2015: 55% MSCI AC World Index, 33% JP Morgan Global Government Bond Index, 7% FTSE EPRA Nareit Global Property, 5% Stefi Call

***Current benchmark

Underlying funds

- FGAM Global Cautious Fund
- FGAM Global Growth Fund
- FPA Global Flexible Fund (Nedgroup)
- Ninety One Global Strategic Managed Fund
- Ninety One Global Franchise Fund

Performance statistics

	Fund	Benchmark
Highest 12-month performance	40.26%	34.52%
Lowest 12-month performance	-16.99%	-15.05%
% positive months	56.38%	59.26%

*Source until 31 May 2018: Iress

Source from 30 June 2018: Morningstar

The FG SCI International Flexible Fund of Funds returned +8.88% in the second quarter of 2023 and +23.86% over the past 12 months, underperforming the benchmark peer group average quarterly return of +9.16% and the 12-month return of +24.34%. The Ninety One Global Strategic Managed Fund was the worst-performing underlying fund over the quarter, returning +3.74% in rand terms. No changes were made to the fund over the quarter.

Asset allocation as at 31 May 2023

	Global Equity	Global Fixed Income	Global Cash	Global Property	Local Cash
FG SCI International Flexible FoF	66%	23%	7%	2%	2%

	USD	GBP	EUR	JPY	Other	ZAR
Currency Breakdown	68%	2%	8%	7%	13%	3%



MARKET PERFORMANCE

Index	Asset Class	Q3 2022	Q4 2022	Q1 2023	Q2 2023	Last 12 months	Year to Date 2023*
STEFI Composite Index	Local cash	1.35%	1.57%	1.75%	1.92%	6.76%	3.70%
FTSE/JSE All Bond (total return)	Local bonds	0.60%	5.68%	3.39%	-1.53%	8.23%	1.81%
FTSE/JSE SA Listed Property (total return)	Local property	-3.54%	19.31%	-5.05%	0.66%	10.00%	-4.42%
FTSE/JSE Africa All Share (Total Return)	Local shares	-1.92%	15.16%	5.17%	0.66%	19.58%	5.86%
JP Morgan World Govt Bond index (USD)	Global bonds	-7.15%	3.84%	3.08%	-2.21%	-2.82%	0.80%
FTSE EPRA Nareit Global REITs TR USD	Global property	-10.84%	6.89%	1.66%	0.94%	-2.19%	2.62%
MSCI World GR USD	Global shares	-6.08%	9.89%	7.88%	7.00%	19.13%	15.43%
MSCI ACWI GR USD	Global shares	-6.71%	9.88%	7.44%	6.35%	17.13%	14.26%
US dollar/South African rand (+ weaker rand, - stronger rand)	Exchange rate	9.71%	-5.33%	4.28%	6.47%	15.31%	11.03%

*(Return until 30 June 2023)



ADDITIONAL FUND INFORMATION

Fund name	No. of participatory interests*	NAV (month-end)*	Total expense ratio (TER)**
FG SCI International Flexible FoF A	15,044,696.09	36.59	1.54
FG SCI International Flexible FoF A1	22.68	35.76	2.1
FG SCI International Flexible FoF B	48,075.18	29.30	3.21
FG SCI International Flexible FoF B1	2,153,870.91	30.33	2.98
FG SCI International Flexible FoF C	7,045,059.97	35.83	1.68
FG SCI Jupiter Income FoF A	41,355,054.64	12.48	1.04
FG SCI Jupiter Income FoF A1	55.02	12.44	1.6
FG SCI Jupiter Income FoF B	8,298.55	12.34	2.77
FG SCI Jupiter Income FoF B1	3,799,118.47	12.37	2.48
FG SCI Jupiter Income FoF C	39,029,095.17	12.29	1.21
FG SCI Mercury Equity FoF A	4,343,257.54	43.60	1.59
FG SCI Mercury Equity FoF A1	16.92	43.49	2.11
FG SCI Mercury Equity FoF B	121.38	41.62	3.31
FG SCI Mercury Equity FoF B1	45,558.51	42.60	3.03
FG SCI Mercury Equity FoF C	295607.52	43.15	1.75
FG SCI Neptune Growth FoF A	25,899,002.50	15.55	1.87
FG SCI Neptune Growth FoF A1	48.67	15.51	2.4
FG SCI Neptune Growth FoF B	65.17	15.38	3.59
FG SCI Neptune Growth FoF B1	1,251,095.35	15.41	3.3
FG SCI Neptune Growth FoF C	1973797.34	15.42	2.04
FG SCI Saturn Moderate FoF A	44,001,840.09	34.83	1.57

* NAV (Mo-End) and no. of participatory interests as at 30 June 2023

**TER as at 31 March 2023



ADDITIONAL FUND INFORMATION

(CONTINUED)

Fund name	No. of participatory interests*	NAV (month-end)*	Total expense ratio (TER)**
FG SCI Saturn Moderate FoF A1	21.24	34.71	2.11
FG SCI Saturn Moderate FoF B	124,833.91	34.41	3.29
FG SCI Saturn Moderate FoF B1	4,601,405.59	34.46	3
FG SCI Saturn Moderate FoF C	10,260,336.75	34.29	1.75
FG SCI Venus Cautious FoF A	68,533,232.02	18.87	1.273
FG SCI Venus Cautious FoF A1	38.22	18.82	1.82
FG SCI Venus Cautious FoF B	30,970.44	18.60	2.9991
FG SCI Venus Cautious FoF B1	5,969,726.35	18.62	2.7132
FG SCI Venus Cautious FoF C	15,187,188.07	18.56	1.31

* NAV (Mo-End) and no. of participatory interests as at 30 June 2023

**TER as at 31 March 2023



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TRANSPARENT
COMPETENT

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