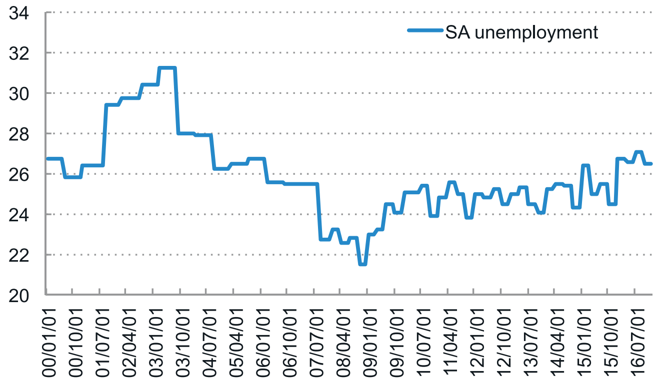
Sanlam

investment strategy
Q1 | 2017

THE ECONOMY

- Eurozone manufacturing PMI sends the stongest signal of economic expansion since April 2011.
- European consumer prices rise 2% year-on-year.
- UK unemployment hits the lowest rate since 1975.
- US CPI is up 2.7%, the most in four years.
- Chinese factory prices rise 7.8% from a year earlier.
- SA posts a trade deficit for 2016, but the current account deficit narrows to its lowest level in six years.
- SA unemployment stands at 26.5% - 2% higher than a year ago.
- SA GDP contracts by 0.3%.
- SA consumer prices rise by 6.3% year-on-year and PPI by 5.6%.
- Malusi Gigaba replaces Pravin Gordhan as SA's minister of finance.

Official SA unemployment rate

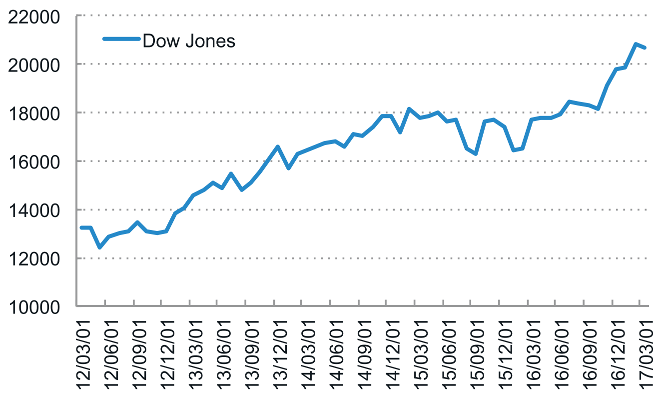


Source: I-Net | Mar 2017

EQUITIES

- The former African Bank starts trading again under the name African Phoenix.
- S&P downgrades Cell C to D, the lowest rating for a corporate company after it misses interest payments.
- Naspers' associate Tencent is now among the top 10 shares globally and the largest emerging markets stock.
- The growth in headline earnings by SA banks is at a 7-year low.
- The ALSI gains 3.8% during the quarter on a total return basis, with Consumer Goods and Services outperforming.
- The SWIX is up 3.0% over the quarter.
- The Dow Jones, S&P and Nasdaq hit fresh records on positive sentiment following Trump's promises. The Dow breaks through the 21 000 level.
- The MSCI World Index (US$) returns 6.5% on a total return basis.
- Emerging markets have an exceptional quarter, gaining 11.5% in US$.

Dow Jones breaks through 21 000 level

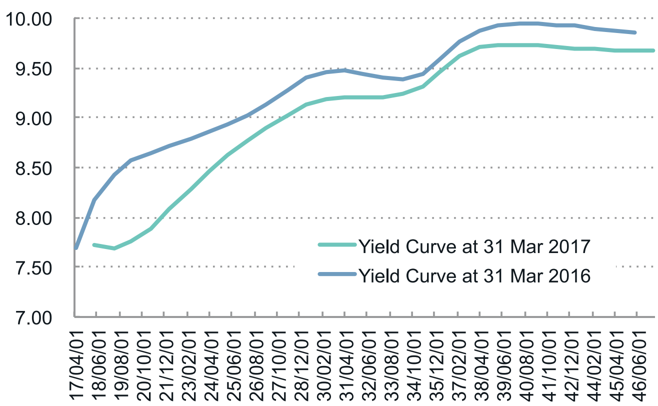


Source: I-Net | Mar 2017

FIXED INCOME

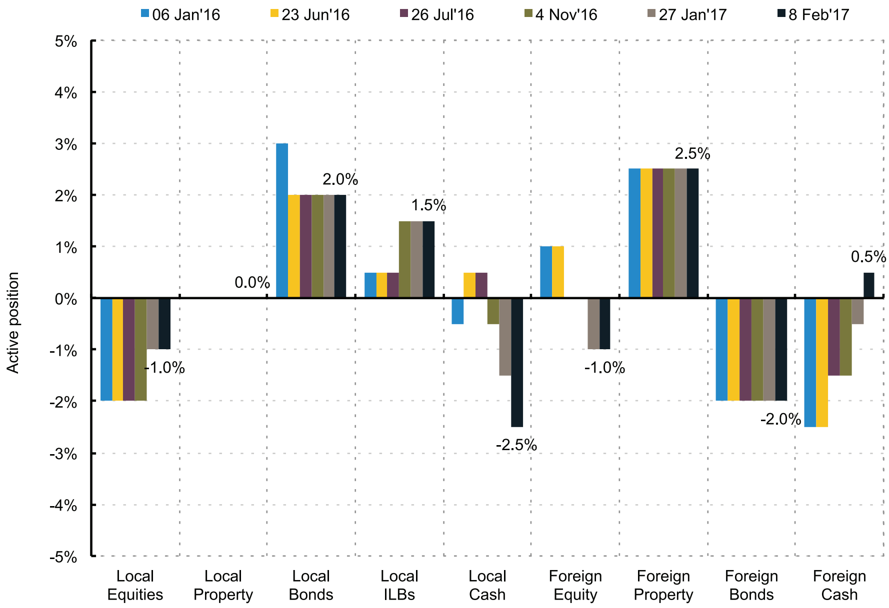
- The Fed raises the federal funds target rate to 0.75-1.0%. The slope of the hike path remains gradual. The median projection for the federal funds rate shows an increase to 1.4% at the end of 2017.
- The ECB allots the final round of its zero-interest loans.
- National Treasury buys back short-dated bonds and issues long-dated bonds as part of its debt maturity management, steepenening the yield curve.
- The SARB keeps the repo rate unchanged and signals it's likely reached the end of its interest rate hiking cycle.
- S&P downgrades SA foreign currency debt to non-investment grade ('junk').
- The SA bond market sees inflows of R19 billion in March.
- SA nominal bonds gain 2.5% during Q1.
- SA inflation-linked bonds return -0.6% vs. the 1.9% from cash.
- Local listed property returns 1.4% for the quarter.

SA: the yield curve steepens



Source: I-Net | Mar 2017

SIM ASSET ALLOCATION



During Q1 2017:

- In January we introduced a 1% underweight position in global equities in favour of global cash and decreased our underweight position in SA equities by 1% from SA cash.
- Early in February we increased our offshore exposure from an underweight to a neutral position by increasing our international cash position by 1%, funded from SA cash.

Source: Sanlam Investments (Mar 2017)

DOMESTIC	POSITION	RATIONALE
Local equities	Underweight	We reduced the size of our underweight position, as we believe the SA market has become less overvalued relative to developed equity markets. The SWIX trades on a current price to earnings (PE) ratio of 15. Given earnings forecasts the PE ratio could drop to about 13 in a year's time. On a price to book basis our market has dropped from 2.8 in 2015 to a current level of 2.3.
Local bonds	Overweight	We retained our overweight in SA long bonds. The real yield on offer remains attractive relative to that of other developed and emerging markets. Part of the high yield can be ascribed to political risk.
Inflation-linked bonds	Overweight	We retained our overweight position. Ten-year inflation-linked bonds (ILBs) currently offer an attractive real return of 2.15%. 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 6.4%, 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 introduced an underweight in global equities in January as markets have rallied since the US elections. The Graham & Dodd PE ratio 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. However, European equities remain cheap and we continue to hold an overweight position in Europe.
Global bonds and cash	Underweight	We retained our underweight position. At a yield of 2.4% US long bonds offer a positive real return relative to our long-run inflation assumption of 2%, but we are concerned about long-run global inflation and now require an attractive premium above 2%.
Global property	Overweight	We retained our overweight position via listed REITs. Our portfolio currently consists of nine companies that have properties in the US, UK, Europe and Australasia. The average dividend yield of the portfolio is 5.7%. Rising bond yields do mean the cost of funding would increase over the longer run, but we also expect some earnings growth from these companies.