Metropolitan Managed Fund

February 2012

The management team of this fund changed on 01 August 2011.

Fund Managers

PSG Asset Management

Neels van Schaik

B.Com (Econ) (Stel); CFA

Adrian Clayton

B.Soc Sc. (UCT);
PDM (UCT);
MBL (UNISA)

Portfolio Information

Portfolio value:	R83.1 million
Original buying price:	95.00 cents
Minimum Investment:	R5 000 lump sum or R500 monthly debit order
Manager's upfront charge (max):	0.00% (incl. VAT)
FSP upfront comm (max):	0.00% (incl. VAT)
Annual service fee:	1.54% (incl. VAT)
Formation date:	13/02/1998
Date of income declaration:	31 Dec/30 June
Date of income payment:	7 Jan/7 July
2010 distribution:	4.98 cpu
2011 distribution:	3.50 cpu
Benchmark:	CPI + 5% over a 2 year rolling period
Risk:	Moderate
Fund Classification:	Domestic Prudential Variable Equity
Valuation and Transaction time:	15h00

Performance Fee:

20% (sharing rate) of out performance above the portfolio benchmark (hurdle rate) , over a 2 year rolling period, capped at 2% p.a. The fees are accrued on a daily basis and paid out on a monthly basis. Any shortfall to the hurdle rate and high water mark is carried forward for set-off against future positive out performances. Fee example: 0% performance fee if portfolio performs in line with its benchmark.

Total Expense Ratio: 1.76%

Please note: the TER has been calculated using data from 1 January 2011 until 31 December 2011. The TER is disclosed as % of the average Net Asset Value of the portfolio that were incurred as charges, levies and fees related to the management of the portfolio and underlying portfolios. The TER is adjusted for significant subsequent portfolio restructurings and/or fee changes. A higher TER ratio does not necessarily imply a poor return, nor does a low TER imply a good return. The current TER can not be regarded as an indication of future TER's.

Investment Objective

The primary objective of the Metropolitan Managed Fund is to offer investors moderate to high long term total returns.

Asset Allocation

	Current	Benchmark
Domestic Stocks	28%	55%
International Stocks	16%	14%
Total Stock Exposure	44%	69%
Preference Shares	0%	0%
Property	0%	0%
Domestic Bonds	7%	10%
Domestic Cash	43%	10%
International Cash & Other	6%	11%
Total Fixed Income Exposure	56%	31%

Top Holdings

Supergroup	4.8%
Tesco PLC	3.9%
Kagiso Media Limited	3.8%
Microsoft	3.6%
Anglo American	3.2%
Sasol	2.3%
MTN Group	2.3%
Steinhoff International Holdings	2.0%
JPMorgan	1.9%
Eqstra	1.9%

Annualised Performance

as at 29 February 2012

	Fund	Benchmark
1 year	4.46%	10.21%
3 years	8.19%	10.42%
5 years	5.37%	11.99%

Investment Strategy

The portfolio will be managed in compliance with prudential investment guidelines for retirement funds in South Africa. In order to achieve its objective, the investments normally to be included in the portfolio may comprise a combination of assets in liquid form, money market instruments, bonds, debentures, corporate debt, equity securities, property securities, preference shares, convertible equities, derivatives, non-equity securities and any other securities which are considered to be consistent with the portfolio's primary objective and the Act or the Registrar may allow from time to time, all to be acquired at fair market value. The portfolio may from time to time invest in financial instruments, in accordance with the provisions of the Act, and the Regulations thereto, as amended from time to time, in order to achieve the portfolio's investment objective. The manager may also include unlisted forward currency, interest rate and exchange rate swap transactions for efficient portfolio management purposes.

Deposits can be made at any ABSA Bank

Account Number:	360 000 931
Bank Code:	31 21 09
Bank:	ABSA
Please fax deposit to:	(021) 940 4856

Custodian: Standard Executors & Trustees: Tel (021) 401-2286. Metropolitan Collective Investments Limited Parc du Cap Mispel Road Bellville, PO Box 925 Bellville 7535 Tel (021) 940-5981

Fax (021) 940-5885 Call Centre, Tel: 0860 100 279 Registration No 1991/03741/06.

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Fund Managers Commentary

Whilst we have only just started managing the Metropolitan Managed Fund, we have been the management team for the PSG Balanced Fund for about thirteen years, clearly a very long time, a period over which the fund has delivered outstanding and consistent returns for the fund's unit holders.

With such a long track record, we have been privy to various investment cycles, with deep stock market dives and extreme gains a common feature. We initiate this month's newsletter with some thoughts on what we have learned managing money and then we reflect on the original investment goals that we set for the PSG Balanced Fund those many years back, which we consider our North Star and which provides ongoing insights to existing and prospective investors as to how the fund is managed.

These exact goals now apply to the Metropolitan Managed Fund, but clearly our involvement is more than a decade later and we like to believe that what we have learned over this period will stand the unit holders of the Metropolitan fund in good stead. We conclude with some brief comments on the fund's current positioning.

Our basic investment views:

- We are of the view that markets move through cycles of under and overvaluation – these can often be extreme.
- We do not believe that markets are perfectly efficient pricing mechanisms.
- Periods of under and over valuation can be protracted.
- Client behaviour is most pronounced during deep market weakness (clients are overly bearish) and excessive market gains (clients are overly bullish).
- At these junctures – markets are unusually cheap or overvalued.
- It is impossible to accurately time market exit points – exiting at highs and entering at lows is pure luck.
- Consequently, we do not believe in market timing and avoid such an approach.
- A fair and statistically accurate assumption to make is that stocks and markets revert to a mean – this allows for long-term clever capital allocation decisions to be made. This is notably different to market timing.
- Working towards or assessing the inherent value within individual companies and then owning or disowning them based on this valuation-based-approach has proven the only successful method to managing money. All the investing greats use such an approach!
- From the points raised above, it is most likely that the managers of the Metropolitan Managed Fund will from time to time (particularly in trending overvalued market cycles) be perceived to be acting in conflict with the desires and interests of our clients.
- It is at these times that client pressure is greatest.
- Whilst client pressure is inevitable, it should not result in any deviation from the consistent application of our investment philosophy and process.
- Existing and future clients should only invest with us if they agree with our value-based investment philosophy and process. They should not invest in this fund based on past performance; no manager can guarantee that past performance will be replicated.
- A cornerstone of our success in managing the PSG Balanced Fund has been a strict adherence to the long-term return objectives that were created for the product at its inception. These objectives are aligned to classical value investing. They are now being applied to the Metropolitan Managed Fund.

On this note, it is worth re-looking at our key investment objectives.

Capital preservation:
The first of which has been to manage the fund in such a manner as to prevent unit holders from experiencing permanent capital losses. We strive to preserve our clients' capital. This is only possible when expensive assets are avoided. Following an approach that circumvents expensive assets can lead to underperforming aggressive competitors that chase markets that are in momentum phases and where assets are overvalued.
Capital preservation must be placed into context; it does not imply that investing into equity-based assets does not lead to negative capital movements over shorter time periods. We distinguish between capital volatility and permanent capital loss. We see no risk in capital volatility, but immense risk in permanent capital loss. Given realistic time periods, our clients will enjoy the rewards that accompany the realisation of value that occurs when quality underpriced assets revalue. We never know how long this process takes. Two key points to take away from this are firstly, that value investing can lead to periods of underperformance and secondly, that returns are not linear and instead usually arise in lumpy clumps requiring patient investing.

Inflation-beating returns:
Our second goal for this fund has been to beat an inflation target of 5%. This is achievable by buying quality businesses with pricing power. Quality companies have the ability to pass inflation on to their consumers. We have also always tried to acquire our assets during mispricing points in the market. Presently however, it concerns us that the behaviour of central banks globally, that have actively participated in markets to buoy them and prevent economic downturns, has resulted in aggressive asset pricing, leading to few opportunities. This has had the further effect that investors have become accustomed to immediate gratification in the form of linear returns. This is quite different to our view that assets more often than not remain dormant for extended time periods with rewards coming in lumpy clumps when least expected.

Beating competitors:
The PSG Balanced Fund is one of the top performing funds within its sector over varying time periods scanning the full 13 years of its existence. Interestingly enough though, over short measurements periods in the past, this fund has gone through stages where it's relative ranking has looked mediocre at best. We have no doubt that we face a future no different to our past. In our view, short-term rankings are a lottery but by applying a disciplined value-based approach that focuses on capital preservation and beating inflation, our long-term ranking will be a certainty. That is our experience so far! We simply have not ever managed funds to beat competitors, it happens naturally when we do things right! We think the Metropolitan Managed Fund will enjoy sound rankings given time!

Some thoughts on our current positioning of the fund:
Our approach has always been to buy quality companies at low prices and let the companies do the work for us. We believe the companies we currently own in the funds we manage, which coincidently are more or less the same as we owned twelve months ago, are all businesses that have the ability to sustain or grow at above inflation levels, their reinvested profits into their underlying businesses. This is for us, the best indicator of the quality of a business. The higher the rate at which a company can reinvest its profits, the higher its long term growth rate and the higher the returns investors should enjoy given time. From this, our unit holders can deduce that our portfolio does not change much and hence they should not expect any radical changes to the portfolio in the immediate future either!

In the past, we found our greatest mistake was selling high quality companies too early; that said, in most instances many of these companies were purchased when the market disregarded their quality. Often we hear the argument made that one should never sell good businesses, whilst we sympathise with this view, the counter argument is equally true, even great companies can be badly overpriced when the market ascribes too much value to future earnings! One great example of this is US retailers; in 2002 Wal-Mart's PE was 37, it is now 13! It has taken a full decade for the company's share price to reach the same levels as in 2002, having fallen 33% from 2002 to its low point in 2007 before beginning a slow and painful grinding recovery. In real terms this is a staggering underperformance.

Domestically we continue to find most large cap quality companies' valuations stretched, those we do own we feel comfortable with at current levels but most new purchases are not large capitalization industrial stocks – this being our normal favourite hunting ground. We also do not believe that where companies are trading at low valuations and low P/E ratings, these are quality businesses that can be fairly compared to quality stocks on higher valuations. Where companies do look 'relatively' cheap, it would seem that this is for good reason! Consequently, at present, we are feeling constrained by high valuations domestically. As we have said often before, this is not the case abroad and we have actively exposed the fund to offshore stocks. We have also bought domestic cyclical stocks when the margin of safety is high enough to offset some of the commodity related risk that accompanies these companies – Anglos and Sasol being our top owned commodity stocks.

Cash proceeds from the limited selling we have done over the last few months has been aimed at purchasing offshore stocks and, to a lesser extent, domestic inflation linked bonds.

In summary, the fund is:

- Well represented with respect to equity exposure, but we are underweight our domestic equity benchmark and actively overweight offshore equities.
- We continue to hold sizeable exposures to cash or cash-like instruments; this will change when meaningful value emerges in the domestic market.
- We are well aware that this asset positioning creates a cash drag effect, but our equity calls have produced high levels of alpha generation and this has offset our defensive asset allocation.
- We feel comfortable with our cash war chest believing that given time, good companies will again be mispriced to the downside which will create favourable entry points.

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