ALLAN GRAY

QUARTERLY COMMENTARY 2

30 JUNE 2013

LONG-TERM THINKING IN ACTION

The cover of this Quarterly Commentary features the Sagrada Família in Barcelona, Spain. Art critics regularly sing its praises, commenting on the uniqueness of its design. And to think it is not even completed yet. Construction of the building commenced in 1882 and the architect Antoni Gaudí dedicated his life to perfecting its unique architectural features. His design was visionary and he would often add details that he knew could only be implemented once the necessary skills and technology had advanced over time. He never gave up on this ambitious project and was still on site when he passed away in 1926. Today, construction continues with the same attention to detail and taking cognisance of Gaudí's vision. The Sagrada Família is expected to be completed in 2026 and reminds us that patience pays off, whether it's a great architectural endeavour or a well-chosen investment.

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ROB DOWER

COMMENTS FROM THE CHIEF OPERATING OFFICER

We have written before about the importance of diversifying your portfolio. Diversification allows you to take individual risks (for example, investments in a country, a class of assets or even a share) that would otherwise not be palatable, since they don't impact the whole of your portfolio. Being able to take on risk, in turn, means the potential for better returns.

Big businesses that operate in South Africa face risks that are not very diversified. For example, many of our retailers, retail banks and insurers serve the same communities of consumers and therefore have in common the risk that their customers may have overstretched themselves in the recent boom in unsecured lending. Similarly, our mines face highly correlated labour and policy risk, and sell their products at correlated commodity prices.

Allocating a portion of your investment offshore spreads your risk across different economies and geographic regions and opens up the possibility of earning returns under different conditions. It also provides the potential to increase returns by offering access to industries and companies that may not be available locally, or that may be performing differently.

Without explicitly intending to do so, this issue of our Quarterly Commentary brings this to light by looking at investment opportunities in Africa and Australia. While these pieces were written by individuals miles apart, they touch on similar themes, and in fact make reference to the same graph – the relative performance of South Africa's key indices. What this highlights is how different sectors can present opportunities at different times; as you broaden your investment universe so these opportunities also increase.

Diversified opportunities in Africa

There is a lot of hype right now about the potential for investment and economic growth in Africa. It is easy to see why. We have always had an embarrassing wealth of minerals. Now, with some progress in bringing these to market and a huge backlog of unmet basic consumer and infrastructure needs, the old problems of political uncertainty, fragmented markets, corrupt bureaucracy and weak governance no longer seem so daunting to commentators. Despite this hype, our analysts are finding opportunities to invest in African markets and these are frequently better priced than their equivalents in South Africa. Almost as importantly, the underlying risks these businesses face are very diverse. For example, it is unlikely that the political and economic risks in Nigeria, Egypt, Kenya or Morocco will coincide. In the short term the prices of their shares may move up or down at the same time according to global fashion. However, for patient investors who have done their homework on the drivers of value and risk in the operations of these companies, correlated short-term price fluctuations represent opportunities and not undiversified risk.

With the Allan Gray Africa Equity Fund celebrating its 15th anniversary, Andrew Lapping and Nick Ndiritu use the opportunity to reflect on the changing landscape over this period and to discuss investment opportunities in Africa in general. While the Fund is not open to South African investors, the Allan Gray Balanced Fund and many of our segregated balanced mandates hold positions indirectly in Africa outside of South Africa.

That is not to say there are no opportunities on home soil. Our clients' largest equity investment is currently Sasol. An analysis of Sasol's long-term performance shows that historically, on average, the market has grossly mispriced the business. This has presented opportunities for us to buy shares at a discount to what we consider to be their fair, intrinsic value. With two very ambitious growth projects under consideration and an undervalued legacy business, Sasol is currently an interesting subject for analysis: in his article this quarter, Rory Kutisker-Jacobson discusses the investment case.

Be aware of the context in which you invest

Regardless of geography, when looking for shares to buy, we look at company-specific attributes, such as the competitive environment and the sustainability of earnings, and we form a view on what a fair price would be to pay for a company's normal earnings. We then compare our estimate of fair value to the company's market price to determine its attractiveness as an investment. We use this same approach locally and in the rest of Africa as do our offshore partner, Orbis, and our sister company in Australia.

This emphasis on philosophy ensures we remain focused and not easily distracted by outside noise. However, we acknowledge that it is important to be mindful of the drivers that influence market prices. Ben Preston, from Orbis, examines one of the biggest investment trends of recent times – the huge and unprecedented decline in bond yields to today's low levels.

Using entrepreneurship to drive job creation

In his update on the Allan Gray Orbis Foundation, Anthony Farr discusses the need to improve South Africa's entrepreneurial pipeline by focusing on young people's perceptions of the opportunities around them, on their capabilities and on their confidence. South Africa's very low level of entrepreneurial activity partly explains why our country has such unacceptably high levels of unemployment, and the Foundation is steadfastly committed to making sustainable changes to this situation.

On the subject of change, our Cape Town head offices will soon be moving into a single building a few hundred metres closer to the city and from early in August you will be able to find us at 1 Silo Square, V&A Waterfront. Our other contact details (i.e. telephone and fax numbers, email addresses and postal address) will remain unchanged.

We remain extremely focused on your investments and thank you for the trust you place in us.

Kind regards

Rob Dower

ANDREW LAPPING & NICK NDIRITU

THE ALLAN GRAY AFRICA EQUITY FUND CELEBRATES 15 YEARS

When the Allan Gray Africa Equity Fund (the Fund) was launched on 1 July 1998 it was the first unitised product in which Allan Gray Proprietary Limited was involved. As the Fund celebrates its 15th anniversary, Andrew Lapping and Nick Ndiritu look back and consider how the market has changed. The Fund is domiciled in Bermuda and invests in South Africa (as well as the rest of Africa), so it is unfortunately not open to South African investors due to exchange control restrictions. The Allan Gray Balanced Fund holds small positions indirectly in Africa outside of South Africa.

The 15-year period prior to the Fund's launch in July 1998 saw a somewhat miserly price return of 2% (annual rate) above inflation for the FTSE/JSE All Share (ALSI). Then, over the next three months, the market fell 22%, erasing the 2% annual gain. At that point, in October 1998, the 30-year real return of the ALSI was 0% excluding dividends.

The experience of equity investors over the 15-year period since 1998 has been somewhat different, with the ALSI price return exceeding inflation by 7% per year. Earnings growth was the primary driver of the recent 15-year returns, with the ALSI earnings growing 12.7% (6.8% real) per year. Put differently, the earnings of the market increased six-fold over the period. This is a very rare occurrence; indeed, as noted above, there have been long periods in South Africa when earnings have failed to grow or have in fact declined. The JSE is not unusual in this regard. Real earnings growth has contributed a little over 1% a year to the return of the S&P 500 over the past 110 years, and not once during that period did real earnings growth average more than 6.5% over a 10-year period, let alone over 15 years.

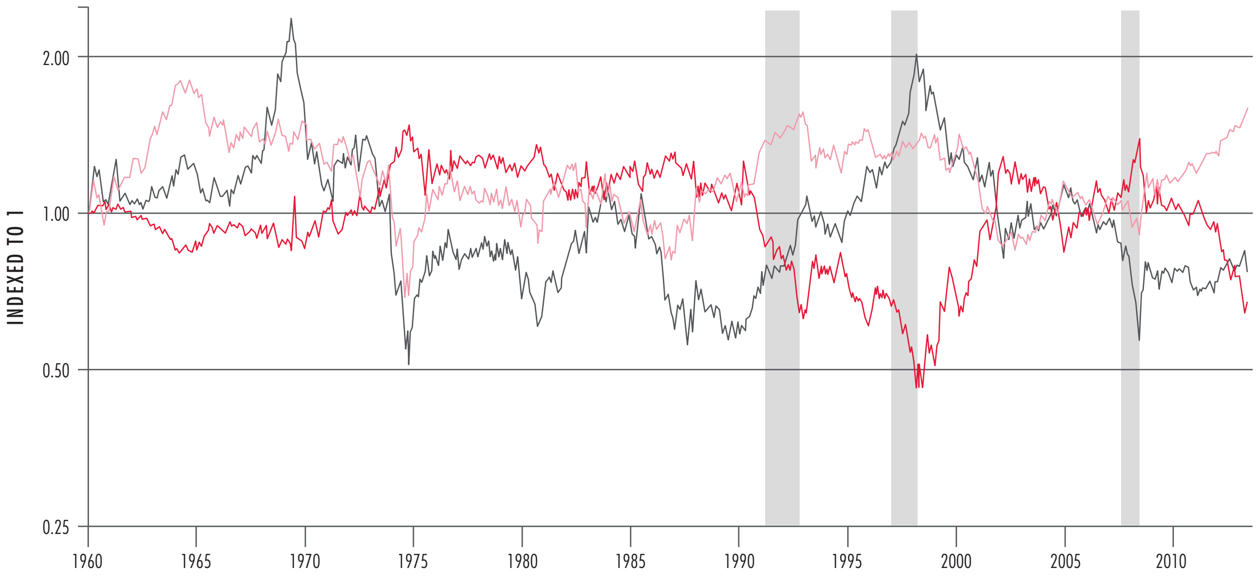
1998: A year of discrepancies

1998 was a period of substantial valuation discrepancy within the JSE, as shown in **Graph 1**. The Resources sector was hugely out of favour, while the Financial sector was loved by investors. As readers familiar with our contrarian investment approach would expect, nine of the Fund's top 10 holdings were in Resources, while the Fund did not hold a single Financial share. Financials, especially the small banks, were seen as the growth sector. In early 1998 the Banking Index traded at 25 times trailing earnings. In contrast, there was substantial value in the Resource sector. Commodity prices were in a bear market, and had been since 1974, and Mining shares were seen as 'old world' compared to the high-flying Financial and IT shares. The multiples on some of the commodity shares were not particularly low, but earnings were very depressed and the holding company structures attracted discounts. So an investor could buy cheap assets through the holding companies which attracted discounts of up to 40%. Almost all of these holding company structures have since disappeared; in fact only two of the original top 10 Fund holdings still exist in the same form.

Some things change, some stay the same

With current high prices it may be difficult to see how assets could ever offer such compelling value as they did in 1998. It is easy to think that things have changed, that investors are smarter and that there will never

GRAPH 1 **INDICES RELATIVE PERFORMANCE**



Source: I-Net Bridge

be similar opportunities again. But it is important to remember that people do not change; this is the one constant of asset markets. It is also important to remember to be patient – opportunities will arise, but they are almost never obvious at the time. When assets are cheap it is usually for what seem to be very compelling reasons. It is only with the passing of time that reasoning may be shown to be accurate or flawed.

We have adjusted the Fund's focus somewhat over the past three years in an effort to find more value opportunities. Up until 2011 the Fund invested practically 100% of its portfolio in South African equities, but we have been steadily moving its asset allocation towards shares listed in other African markets. Only 35% of the Fund's holdings are domiciled in SA at the moment because of the better value we see in shares listed in other African markets. The African companies we are investing in have lower earnings and the multiples investors are placing on these earnings are far more reasonable when compared to South Africa.

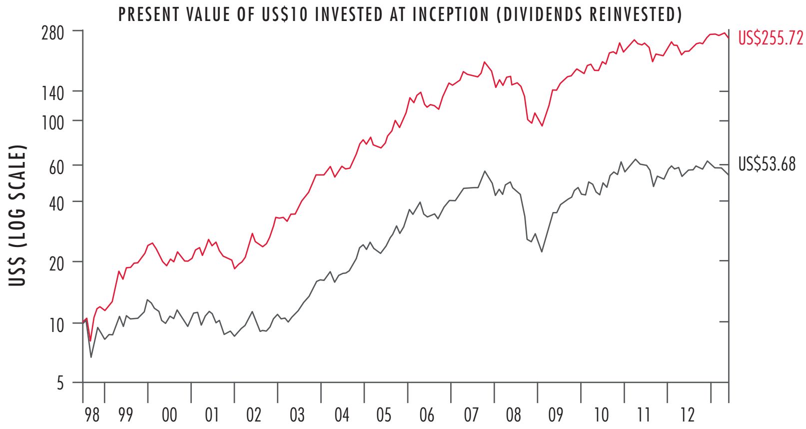
Many investors are very positive on the outlook for African equity markets, excluding South Africa, as the consensus forecast is for strong GDP growth in the medium term. As discussed in Quarterly Commentary 4, 2011, evidence indicates that the correlation between GDP growth and equity market returns is very weak and using GDP forecasts to inform equity allocation is a dangerous business. Being value managers we have increased our allocation to African equities as we are finding better value in these markets when compared to shares listed in South Africa, not because we have a particularly positive outlook on the GDP growth prospects. When looking for shares to buy we look at the company specific attributes, such as the competitive environment and the sustainability of earnings, and we then decide on a fair price for these normal earnings. Using this method we determine a fair value for the share and then compare the fair value to the market value to determine the attractiveness of the investment. As it happens, we are currently finding far more shares trading at a discount to fair value in the rest of Africa than in South Africa.

The pan-African opportunity

The advantage of being able to invest across the African continent is that shares in many African markets are not carefully researched by investors and the markets are very retail driven, so large discrepancies between fair value and market value can open up. Short-term news events often drive the disparities between fair and market value. Across the continent, negative news events and market dislocations are more frequent than if an investor has just one country to choose from. Being contrarian investors we hope to take advantage of the negative sentiment and value opportunities. That said, the consensus is sometimes correct and buying into bad news can result in substantial losses: unfortunately, great investment opportunities are never obvious. However, in our experience, over the long term it pays to be contrarian and take advantage of negative sentiment.

A company that is currently very out of favour is Egyptian gold mining business, Centamin. Centamin owns the low-cost Sukari mine, which should produce about 400k ounces of gold a

GRAPH 2 **THE FUND'S PERFORMANCE NET OF ALL FEES AND EXPENSES**



ALLAN GRAY AFRICA EQUITY FUND[1] BENCHMARK[2]

% RETURNS	FUND	BENCHMARK[2]
Since inception (unannualised)	2 457.2	436.8
Since inception (annualised)	24.1	11.9
Latest 10 years	21.3	16.8
Latest 5 years	11.4	3.3
Latest 3 years	13.6	8.1
Latest 2 years	4.0	-5.5
Latest 1 year	17.5	-1.9
Year-to-date (unannualised)	0.3	-13.9
Risk measures (since inception, based on month-end prices)		
Maximum drawdown[3]	-52.5	-60.5
Percentage positive months[4]	60.6	57.2
Annualised monthly volatility[5]	26.7	28.0

[1] The Fund is currently priced in US dollars. Since inception to 30 April 2012 the Fund was priced in South African rands.
[2] The current benchmark is the MSCI EFM Africa Index (total returns). Since inception to 30 April 2012 the benchmark was the FTSE/JSE All Share Index including income. Performance as calculated by Allan Gray at 30 June 2013 (Source: Bloomberg). Calculation based on the latest available data as supplied by third parties.
[3] Maximum percentage decline over any period. The maximum drawdown occurred from October 2007 to February 2009 and maximum benchmark drawdown occurred from October 2007 to February 2009. Drawdown is calculated on the total return of the Fund/benchmark (i.e. including income).
[4] The percentage of calendar months in which the Fund produced a positive monthly return since inception.
[5] The standard deviation of the Fund's monthly return. This is a measure of how much an investment's return varies from its average over time.

year over its 20-year life. What makes Centamin unique is its position on the cost curve. Once the project to double production is complete later this year, the mine should produce gold for a total cost of US$1 000 per ounce.

This compares to AngloGold Ashanti, Gold Fields and Harmony where the costs exceed US$1 600 per ounce. At US$1 300 per ounce, Centamin should generate free cash flow of US$0.06 per share. The share price is US$0.45 and in addition there is net cash of US$0.18 per share on the balance sheet. Unfortunately companies never trade at these sorts of valuations for no reason. A former Egyptian member of parliament challenged the legality of Centamin's mining rights in the Egyptian Administrative Court and won. Centamin, with the support of the Egyptian Mineral Resources Authority, is appealing the ruling and on our reading has a very strong case as certain crucial evidence was not presented at the original hearing, notably the signed Concession Agreement. There is no certainty in predicting the outcome of a case before an Egyptian court, but looking at the facts and the potential upside versus the downside returns, we think Centamin is an attractive investment opportunity.

The Allan Gray Africa Equity Fund's performance over the past 15 years resulted in substantial wealth creation for investors (see **Graph 2**). These returns are very unusual and cannot be expected in future. What investors can expect is that we will continue to do exactly what we did over the past 15 years, which is value companies based on their long-term fundamentals and invest in those companies that are trading at a discount to fair value.

Prior to 2010 the Fund was managed by our offshore partner Orbis, with Allan Gray only advising Orbis on stock selection. In October 2010 we took over the full investment management responsibility of the Fund.

Andrew joined Allan Gray in February 2001. He is a fund manager for the Allan Gray Bond and Money Market funds, as well as the African equity portfolios, and also manages a portion of client equity and balanced portfolios.

Nick joined Allan Gray in March 2010 and is a member of the investment team with a pan-African focus across equities and fixed income.

RORY KUTISKER-JACOBSON

SASOL: A HISTORY OF UNDERESTIMATION

Sasol is our clients' largest equity investment. Founded in 1950 and listed in 1979, Sasol's core business is to produce synthetic liquid fuels and chemicals, based on its proprietary coal to liquids (CTL) and gas to liquids (GTL) technology. Over time Sasol has expanded its operations beyond South Africa's borders to include, amongst others, chemical plants in Europe and North America, gas assets in Canada and Mozambique, and a GTL plant in Qatar. Rory Kutisker-Jacobson looks at the investment case for the company.

When valuing a company, a standard approach is to apply a multiple to that company's earnings. The earnings multiple one is willing to pay should reflect that company's ability to sustain, and indeed grow earnings. Shares with above-average long-term growth rates deserve higher price-to-earnings (PE) multiples and vice versa.

Since 1980, the PE multiple on which Sasol has traded has been at an average discount of 20% to the FTSE/JSE All Share Index (ALSI), and often as high as 40%. This implies that historically the market has considered Sasol a below-average business, with inferior growth prospects. Sasol's earnings are highly dependent on the rand and the dollar price of oil, both of which can fluctuate wildly and are beyond the control of management. This makes Sasol's year-on-year change in earnings unpredictable and cyclical. One must be wary of confusing cyclicality with inferiority though, as through the cycle a company may still be very profitable when the good and bad years are added together.

An analysis of Sasol's long-term performance suggests that historically, on average, the market has grossly mispriced the business. **Graph 1** on page 7 shows the earnings of Sasol relative to the ALSI rebased to 1. Since 1980, Sasol has grown its earnings at a compound annual rate of 15.9% versus the market's growth rate of 11.7%, whilst maintaining a 'payout ratio' (**see textbox**) similar to that of the market. Shareholders in Sasol who invested in 1980, would now be receiving dividends three times greater than the average dividend on the ALSI. It is not often one finds a stallion selling for the price of a donkey.

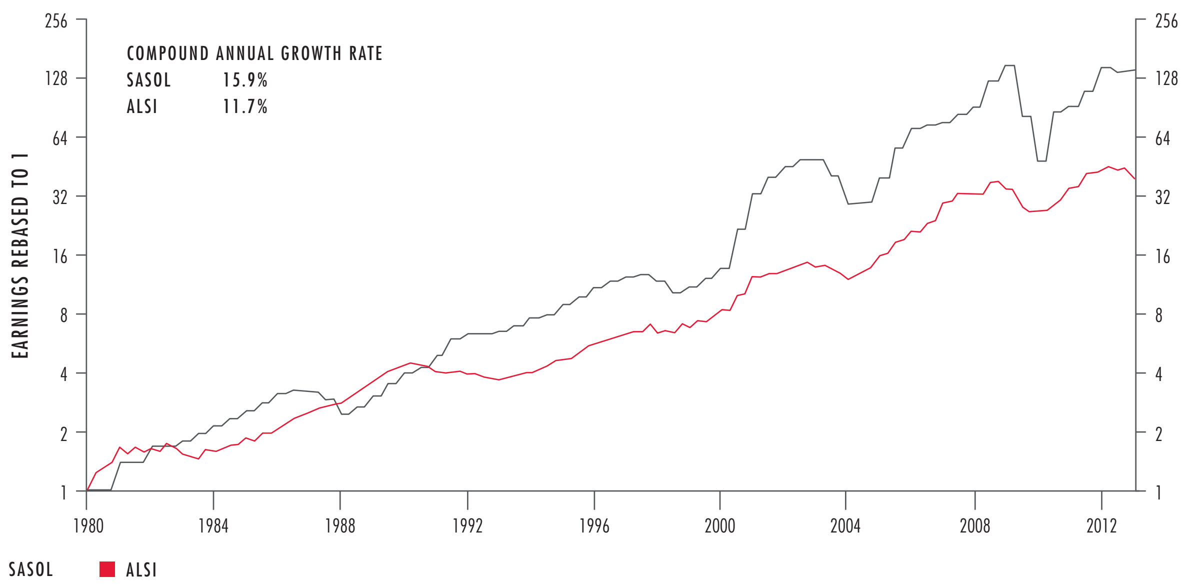
The normal oil price

As mentioned above, the most important determinants of Sasol's earnings are the rand and the dollar price of oil. When valuing Sasol, it is thus important to have an estimate of what a normal rand oil price is. **Graph 2** on page 8 shows the price history of oil in real and nominal terms since 1861. It is hard to argue that the current oil

Payout ratio

The 'payout ratio' is the portion of earnings paid out in dividends to shareholders. A company which is able to pay out a greater proportion of its earnings, while still maintaining an equal or superior rate of growth to the market, would be considered a higher quality company.

GRAPH 1 **SASOL VS ALSI – EARNINGS REBASED TO 1**



Sources: I-Net Bridge, Company reports

price of US$103 per barrel is low by historical standards.

The question then becomes: Why is the oil price high, and, more importantly, is a significant decline in the future likely?

Unlike many commodities, the oil market is somewhat unique in that the swing producer is one of the lowest cost producers. Roughly 43% of world production comes from the Organisation of the Petroleum Exporting Countries (OPEC), with Saudi Arabia being the largest producer. Saudi Arabia is also the only OPEC country with significant spare capacity. While the pure cost of extraction in Saudi Arabia is low, the vast majority of government revenue is derived from the sale of oil, which is used to subsidise other industries and social welfare. Current estimates are that Saudi Arabia needs an oil price of between US$90 and US$100 per barrel to balance its fiscal budget. It is in the Saudis' best interests to manage the supply of oil to maximise their revenue per barrel without encouraging demand destruction.

Outside of OPEC, the future supply growth of oil will increasingly come from offshore ventures, more geographically risky areas and unconventional sources such as GTL, Canadian tar sands and shale oil. Future oil prices will probably need to be higher than those of the past to meet the higher cost of bringing these projects on stream. At present, the marginal cost of producing oil from unconventional means is estimated to be between US$80 and US$90 per barrel. In the long term, the marginal cost of supply typically sets the price at which that commodity trades.

We cannot predict the future, and we do not know what the price of oil will be in a week, a month or a year. However, we believe the above arguments provide sound structural reasons why the oil price is unlikely to fall below a real price of US$80 per barrel on a sustainable basis over the long term.

Similarly, we cannot predict the future value of the rand. However, we believe that given the inflation differential between South Africa and the USA, over the long term the rand is more likely to weaken than strengthen. A weak rand is bad for the local consumer, but favourable for Sasol.

For the year to June 2013, consensus expectations are that Sasol will earn around R45 per share. At the 28 June closing share price (R432 per share), Sasol is thus trading on less than 10x earnings, compared to the ALSI's PE multiple of 16.4x. With oil averaging R960 per barrel, the last year has been a favourable trading environment for Sasol, and earnings are arguably high. We estimate that Sasol would earn approximately R36 per share at a lower oil price of R760 per barrel. Even then, Sasol's PE would be closer to 12x, still well below that of the ALSI.

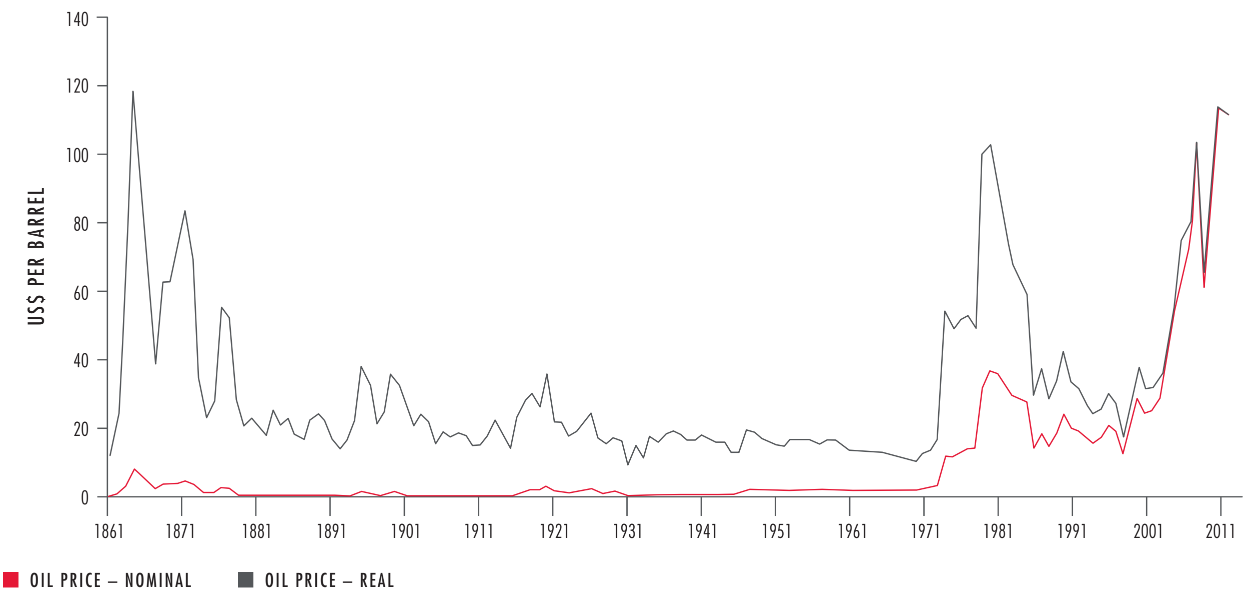
Once again the market appears to be discounting very poor earnings growth expectations into Sasol's share price relative to the average company. Is the market right this time?

Sasol's growth prospects

Sasol is considering very ambitious growth projects, which, if successfully completed, will see the company's total production volumes on a barrel of oil equivalent basis increase by more than 50%.

The two largest projects under consideration are an ethane cracker,

GRAPH 2 **CRUDE OIL PRICES: 1861-2012**



Source: BP Statistical Review 2012

at an expected cost of between US$5bn and US$7bn, and a GTL plant, at an estimated cost of between US$11bn and US$14bn, funded via a combination of debt and internal cash flows. Both are likely to be situated near their existing facilities in Louisiana, USA. Sasol is currently undertaking the preparatory work to determine the exact design, costs and expected economics of these projects. The logic behind both plants is compelling. Essentially, Sasol will buy cheap gas as feedstock and using its technology, convert it into petrochemicals and liquid fuels, which are linked to the price of oil. **Graph 3** on page 9 shows the historical correlation between the price of oil and the gas price in the USA. Until recently, the Brent oil price traded at roughly 10x the Henry Hub gas price. From 2009 onwards however, advances in the technology of horizontal drilling have seen an explosion in gas production, as previously unavailable shale gas can now be viably extracted, resulting in excess supply and low prices. This has caused the price relationship between oil and gas to alter structurally. Given the abundance of shale gas reserves and potential available supply, even if a number of new markets are developed for this gas, the relationship is unlikely to revert to historical levels.

A final investment decision is expected on the ethane cracker in 2014, with beneficial operation commencing in 2017. As a final investment decision on the GTL facility is only expected in 2016, let us focus on the economics of the ethane cracker.

Ethylene is produced using either ethane or naphtha as a feedstock. As ethane is derived from natural gas, its price is much cheaper than naphtha, which is linked to the price of oil. This provides ethylene producers who use ethane with a distinct competitive advantage. Sasol is not the only petrochemical company to notice this opportunity, and a number of new plants are under consideration in the USA. Given the existing size and growth of the market however, even if all the plants under consideration proceed as planned, the marginal cost of production will remain materially higher than Sasol's own cost. We think this provides the proposed ethane cracker with a sufficient margin of safety. **Graph 4** on page 9 shows the global cost curve for ethylene producers and the expected cost curve in 2018 if all the proposed ethane crackers in the USA are constructed.

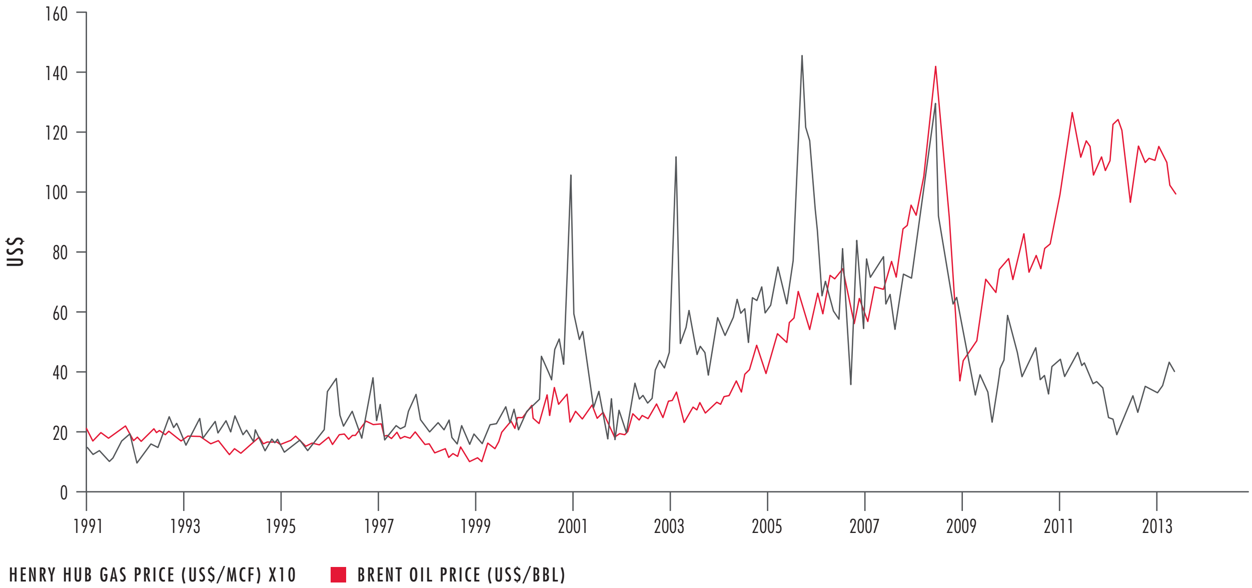
> **"...CURRENT UNCERTAINTIES ARE PROVIDING AN OPPORTUNITY FOR INVESTORS TO BUY THE STRONG EXISTING OPERATIONS OF SASOL AT AN ATTRACTIVE PRICE..."**

Opportunity outweighs risks

Sasol's performance on capital projects over the past few years has been poor, which has caused the market to lose confidence in its ability to deliver on future projects. The large amount of capital involved on the US projects has given investors further cause for concern. Combined, we believe these doubts are depressing Sasol's share price more than is warranted.

Importantly, as mentioned earlier, a final investment decision on the larger of the two projects, the GTL plant, will only be undertaken in 2016, far into

GRAPH 3 **US GAS PRICES VS BRENT OIL PRICE**

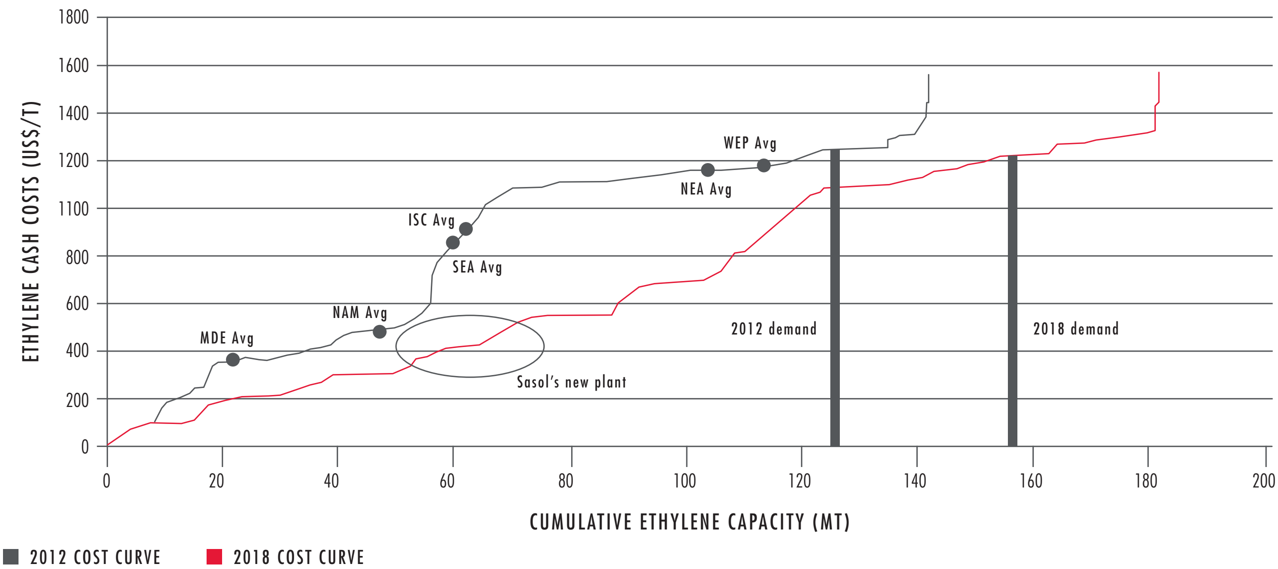


Sources: I-Net Bridge, Bloomberg

the construction of the ethane cracker. Over this time, Sasol's management will thus have gained valuable insight into their actual experience versus original expectations, and be in a position to incorporate this knowledge into the latter investment decision. At this time management will also have greater clarity on the feedstock and product price environment to be expected. In our opinion, this somewhat mitigates the downside risks.

In our view, the current uncertainties are providing an opportunity for investors to buy the strong existing operations of Sasol at an attractive price and gain exposure to its promising potential projects in North America, where we believe the upside opportunity outweighs the downside risks.

GRAPH 4 **GLOBAL ETHYLENE COST CURVE SHOWING IMPACT OF ALL US ETHYLENE PROJECTS**



Note: Based on a West Texas Intermediate (WTI) oil price of US$95/bbl.
MDE = Middle East; NAM = North America; SEA = Southeast Asia; ISC = Integrated Steam Crackers; NEA = Northeast Asia; WEP = Western Europe

Sources: CMAI, UBS

Rory joined Allan Gray as an equity analyst in 2008. He has a Bachelor of Business Science and is a CFA charter holder.

BEN PRESTON

DO NOT CONFUSE STABILITY WITH SAFETY

According to Ben Preston, from our offshore partner Orbis, Orbis and Allan Gray's strict adherence to our bottom-up research process keeps us focused on undervalued companies and ensures we do not spend too much time pontificating on broader investment trends. However, it is helpful to be aware of the drivers that influence market prices. Ben discusses one of the biggest investment trends of recent times – the huge and unprecedented decline in bond yields to today's low levels.

Central bank policy – a help or a hindrance?

Bond yields today are a far cry from conditions in the 1980s, when one could buy a US Treasury bond yielding about 15%. The subsequent return on those bonds has been fantastic – not only because of the high starting yield, but also because yields have come down, which means prices have gone up. This was driven initially by central banks getting high inflation under control, and more recently by their experiments with 'quantitative easing'.

Bond investors have been richly rewarded over the last 30 years. Unfortunately, there is little chance of repeating that experience now: starting yields are just too low.

For example, in March Japan issued a 10-year bond with a 0.6% annual coupon. For every JPY100 invested, a bondholder receives JPY0.6 per year for 10 years, plus the return of principal at the end of the period. Over the life of the bond, cash flows sum to a grand total of JPY106 – which means that, even if bond yields were to go to zero (for the first time in history) the total upside from owning that bond is just 6%.

According to the textbooks, owning a government bond is 'risk-free' and, in today's uncertain world, one can see why investors have been willing to pay a high price for safety. But is it really true to say there is no risk from holding such a bond?

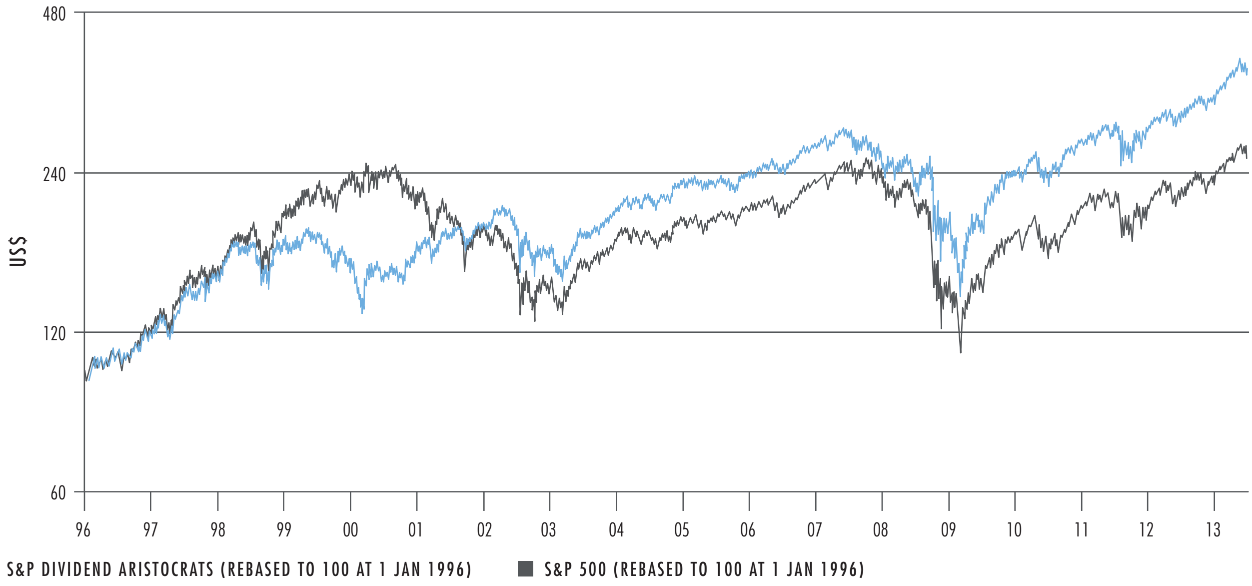
For instance, what would it take for this investment to lose 20% of its value? The answer is that yields would only have to rise to 3% – hardly high by historic standards. If yields climbed to 7.5%, just under the prevailing rate in South Africa today, the Japanese bond would lose about half its value.

"AT ORBIS, WE HAVE ALWAYS TAKEN THE VIEW THAT INVESTMENT RISK – THE RISK OF LOSING MONEY – COMES CHIEFLY FROM OVERPAYING."

What does any of this mean for stock markets?

Given the low yields available on bonds, it is unsurprising that investors have sought other assets with bond-like characteristics. One class of investments that has done well is 'bond proxies': stocks with stable earnings and regular dividends. As an attractive alternative to bonds, such stocks have performed well. By way of illustration, consider the performance of the S&P 'dividend aristocrats' compared to the broader S&P 500, as shown in **Graph 1** on page 11.

GRAPH 1 **S&P 500 VS THE DIVIDEND ARISTOCRATS**



The Dividend Aristocrats index includes S&P 500 components that have raised dividends every year for at least 25 consecutive years.
Source: Datastream

(A 'dividend aristocrat' is an S&P 500 component that increased its dividend every year for at least 25 consecutive years.)

For most of its history, the price return from the dividend aristocrats has been similar to that of the broader index – until the start of quantitative easing in 2009, that is. As bonds rallied, the dividend aristocrats joined in, driving prices to multi-year highs.

All else being equal, the higher the price, the lower the subsequent return. Just as we saw with the Japanese bond, an investment with predictable cash flows can still be risky if the price paid is too high.

Risk versus reward

Compared to bond proxies, we think other shares offer a more attractive balance of risk and reward. One example is NetEase, a Chinese online game developer. The company is a great business, and as internet penetration increases in China, NetEase should be a major beneficiary.

If we compare NetEase to a bond proxy like Coca-Cola, the latter offers more stable and predictable cash flows, and a regular dividend, but NetEase is growing much faster. The comparison becomes more interesting if we include bonds as an alternative. If 10-year bonds were a stock, their dividend would be the yield to maturity, and the growth rate would be zero because the coupon is the same every year. If we treat the coupon as 'earnings', the price-to-earnings (PE) ratio of a US Treasury Bond would be 40 times (see **Table 1**).

Viewed this way, Coca-Cola certainly looks more attractive than US Treasury bonds – it offers a higher dividend yield, potential for earnings growth, and trades at a lower earnings multiple. But NetEase looks better still. While it offers no dividend, that is more than made up for by an earnings growth rate far exceeding Coca-Cola's. Investors typically pay a higher multiple for faster growth, but in the scramble for stability, this has been turned on its head, and NetEase now trades for a lower multiple of earnings than Coca-Cola does.

In our view, buying a fast-growing company at a modest earnings multiple is a more attractive proposition than buying a stable one at a high multiple. This is reflected in the current positioning of the Orbis Global Equity Fund, which is underweight these bond-like shares. During the

TABLE 1 **WHAT IF 10-YEAR US TREASURY BONDS WERE A STOCK?**

	10-YEAR US TREASURY BONDS	COCA-COLA	NETEASE
CURRENT INDICATED DIVIDEND YIELD	2.5%	2.7%	0.0%
EPS GROWTH, LAST 5 YEARS (CAGR)	0%	9%	26%
2013 IBES* P/E MULTIPLE	40x**	18x	11x

*The Individual Brokers Estimate System
**Bond equivalent, calculated as 100/2.49
Sources: S&P Compustat, Datastream, Bloomberg

GRAPH 2 **AIG: TRADING AT AN UNWARRANTED DISCOUNT TO PEERS**

P/TNAV: Price to tangible net asset value
Sources: Datastream, Orbis

past few years, many of our favourite stocks have endured periods of underperformance as investors have bid bond proxies up to historic highs.

At the other end of the spectrum, there are stocks available at what we believe are more compelling prices. One example is US insurer AIG. Today, AIG's tangible net assets are worth about US$60 per share, and the company targets a return on equity of at least 10% over the long term. Should the company deliver, this would result in US$6 of earnings per share, giving an earnings yield of about 15% at current prices.

In a world looking for consistency and stability, it seems AIG has been widely overlooked. AIG's woes during the recent financial crisis have been very well documented, but we believe that it is a different company today, with a different management team and a different mix of businesses. Crucially, this does not appear to be reflected in the company's valuation.

Graph 2 looks at the price to tangible net asset value (TNAV) of US insurers. The average US insurer has historically commanded a premium to TNAV. Even the 20th percentile insurer – the 'top end of the bottom 20%', one might say – has typically traded around or above TNAV. AIG sits right at the bottom of the chart.

Why is the price so low?

Today, AIG's earnings are below where they should be. It may take a long time for the company's return on equity to reach management's 10% target, so the stock is of little interest to investors with a short time horizon. But over the long term, we believe AIG represents a compelling balance of risk and reward. Amid the stock market's current preference for stability, AIG's past reputation for instability counts against it. But we would caution investors not to confuse 'stability' with 'safety'. There is nothing wrong with stability of course. But no investment is safe, no matter how stable the underlying company, if you pay too much for it.

At Orbis, we have always taken the view that investment risk – the risk of losing money – comes chiefly from overpaying. While our approach is not always in sync with the market, history suggests that investment fashions come and go – whether it is high growth or high tech or high predictability. Following the investment fashion of the day may feel comfortable, but it is not conducive to generating superior long-term returns for our clients. We have learnt to be comfortable being uncomfortable.

Ben is a director of Orbis Investment Advisory Ltd. He joined Orbis in 2000 and his primary responsibility is researching global equities in the consumer and financial sectors.

JD DE LANGE & LJ COLLYER

EQUITY OPPORTUNITIES DOWN UNDER

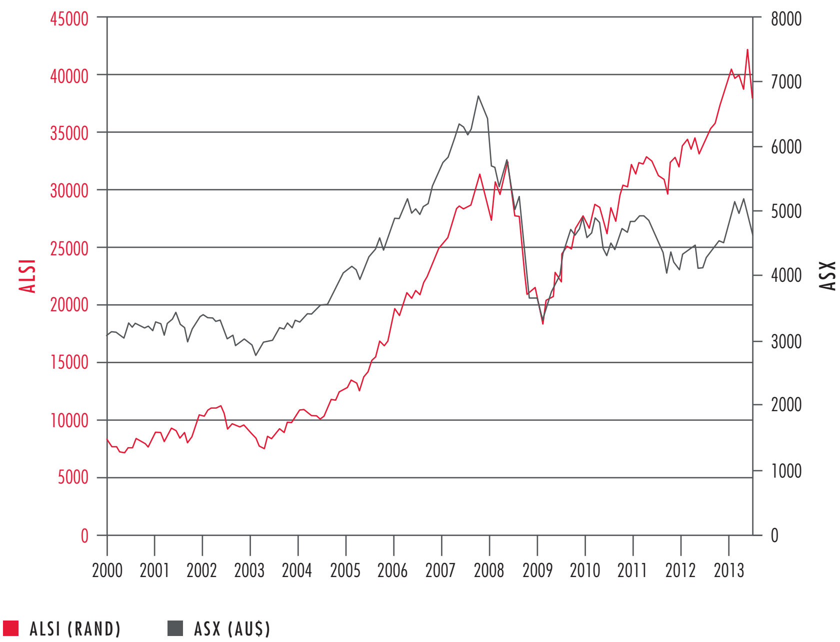
Last quarter, Seema Dala wrote about the importance of diversifying your portfolios by investing offshore. Australia is definitely offshore from South Africa, but there are also some strong similarities between the two economies. LJ Collyer and JD de Lange, from Allan Gray Australia, examine whether investing in Australian equities makes sense for a South African investor.

Other than being fierce competitors on the sports field, South Africa and Australia have many other things in common. For the 112 years to the end of 2012, for example, South Africa and Australia had the best performing stock markets in the world, in real terms[1]. Both are resource-rich countries, and resource companies make up a significant percentage of both the Australian Stock Exchange (ASX) and the Johannesburg Stock Exchange (JSE). Furthermore, financial shares make up more than 30% of both the S&P/ASX 300 Index and the FTSE/JSE All Share Index (ALSI). In terms of contribution to global GDP, South Africa contributes less than 1% and Australia 2-3%.

Despite a similar make-up, the indices show stark differences in valuation

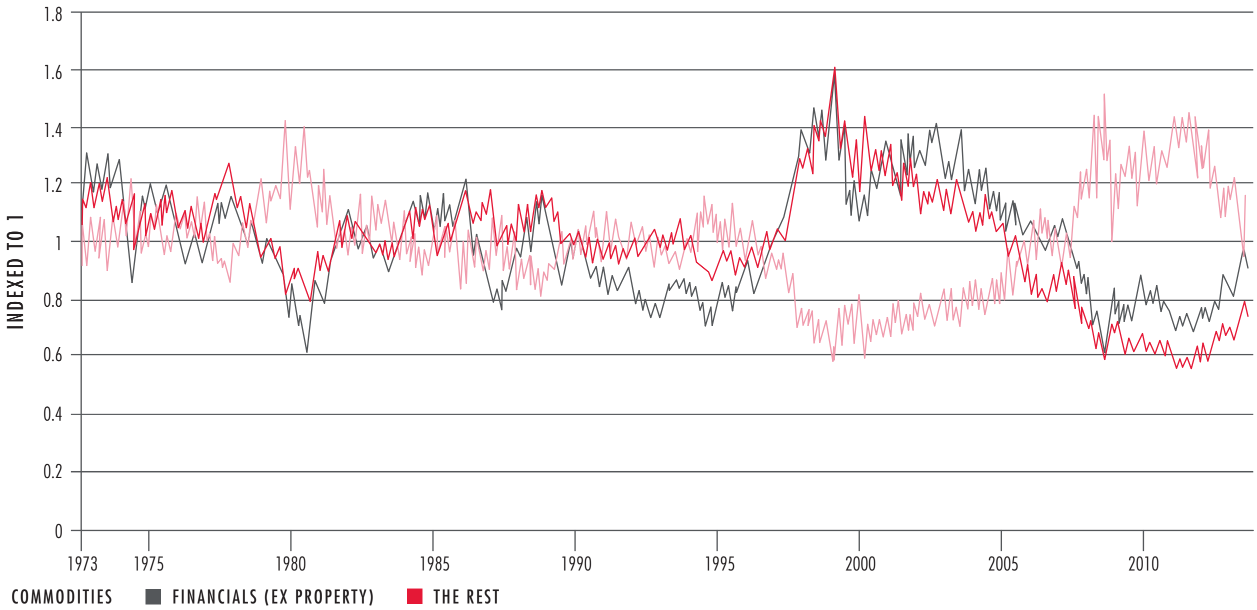
Since the 2008 global financial crisis, the South African market has rebounded, recording new highs in 2013. The Australian stock market, meanwhile, has not seen this type of recovery. Although last year was a good one for Australian stock market investors, there are still a lot of stocks trading below our estimate of intrinsic value. **Graph 1** displays the performance of the two indices since 2000 in local currency terms (the ALSI

GRAPH 1 **SOUTH AFRICAN AND AUSTRALIAN STOCK MARKET PRICE INDICES**



Source: I-Net Bridge

GRAPH 2 **AUSTRALIAN SECTOR RELATIVE PERFORMANCE**

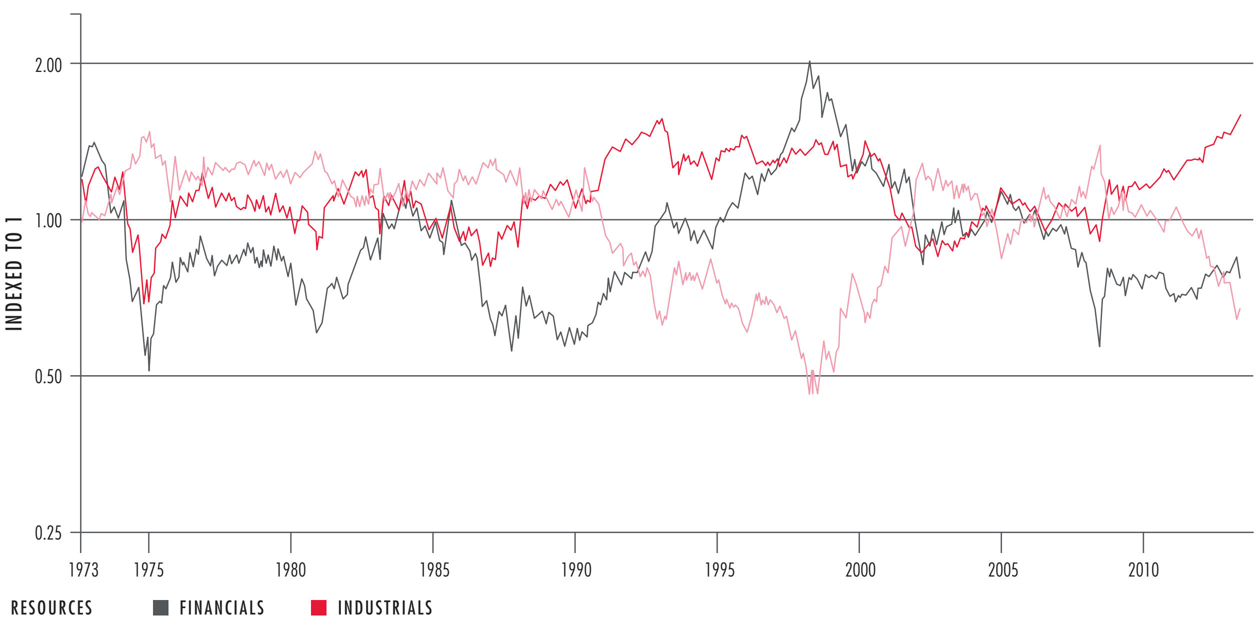


Sources: Allan Gray Australia Research, IRESS

on the left hand axis and the ASX on the right).

The valuations between the two countries are not aligned and the sectors where one can find value are also different. Compare **Graph 2**, which shows the relative performance of key indices in Australia, to **Graph 3**, which illustrates the South African story. Australia's Retail sector has been trading at cyclical lows over the last few years due to cheap imports from China, growing online competition, a high savings rate and competition for capital from a Commodities sector that has excelled until recently. The picture is quite different in South Africa, where retailers (and other industrial shares) have been booming, while the Commodities sector has had a torrid time on a relative basis. These differences suggest a range of diversification opportunities for South African investors.

GRAPH 3 **SOUTH AFRICAN SECTOR RELATIVE PERFORMANCE**

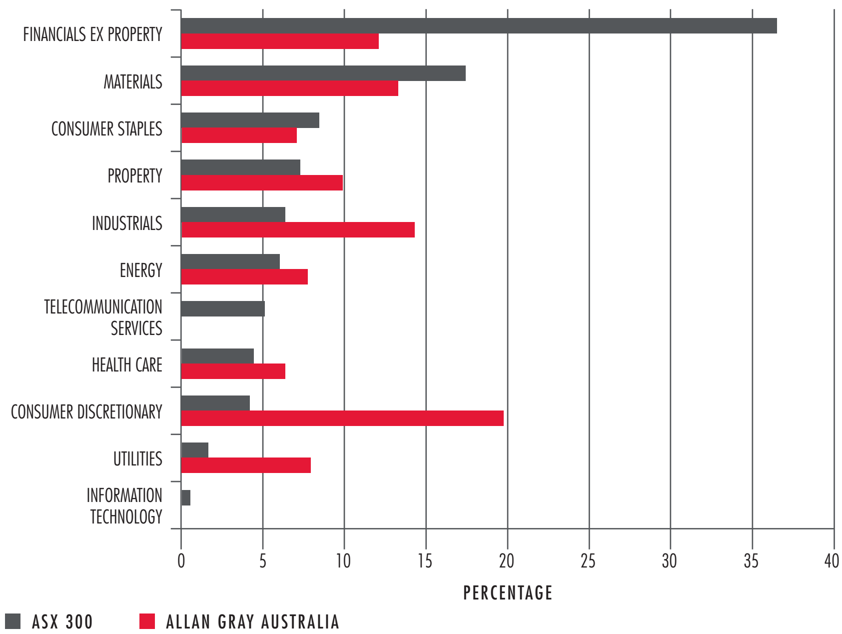


Sources: I-Net Bridge, Allan Gray Research

The Allan Gray Australia Equity Fund is typically contrarian, which in itself provides diversification

Looking at the sectors that have underperformed (as shown in Graph 2), readers who are familiar with our contrarian approach to investing will not be surprised that the Allan Gray Australian Equity Fund is very underweight Commodities and Financials (that together represent 55% of the ASX). As a result, the Fund has a very large exposure to the rest of the ASX. The current positioning of the Fund compared to the ASX 300 is shown in **Graph 4**. The Fund therefore offers South African investors a fair degree of diversification on a sector level.

GRAPH 4 **SECTOR ALLOCATION OF THE ALLAN GRAY AUSTRALIA EQUITY FUND VS THE ASX 300 AS AT 30 JUNE 2013**



Source: Allan Gray Australia Research

In addition, a number of the top 10 shares held in the Fund are in sectors that provide unique opportunities to South African investors because they are lesser known sectors or similar opportunities are not available on the JSE. Examples of these include:

- Utilities – SP AusNet (7.7% of the Fund): A utility company that manages an electricity and gas network in Victoria, Australia, providing electricity transmission and distribution and gas distribution services to households and industry.
- Energy – Origin Energy (4.1% of the Fund): Australia's largest energy retailer and one of the country's largest electricity providers. It also has significant interests in liquefied natural gas (LNG) projects and invests in a number of renewable energy technologies.

Investing in Australian equities via the Allan Gray platform

One way for South African investors to access Australian shares is through an Australian equity fund, either directly through an Australian investment manager, or by investing in a fund via an offshore platform. The Allan Gray Australia Equity Fund seeks to offer investors an opportunity to benefit from higher long-term returns than the Australian stock market as measured by the S&P/ASX 300 Accumulation Index. It is a concentrated portfolio of shares listed on the ASX and may be appropriate for investors looking for contrarian-style investment exposure to the Australian stock market. Investors must be able to take a long-term view and endure shorter-term performance fluctuations. A minimum investment period of five years is recommended. Investors looking for investment exposure to Australia, without taking on equity market risk, should follow the same approach as they would when picking a local fund, and look for funds that are not as exposed to the equity markets.

> **"FOR THE 112 YEARS TO THE END OF 2012 ... SOUTH AFRICA AND AUSTRALIA HAD THE BEST PERFORMING STOCK MARKETS IN THE WORLD, IN REAL TERMS[1]."**

The Allan Gray Australia Opportunity Fund invests in top-rated Australian bank deposits. In addition, analysts look out for investment opportunities in the Australian stock market where they have high confidence that a specific share will yield returns better than cash with limited downside. Over the long term the Fund aims to deliver a return better than the Australian Reserve Bank's cash rate, rather than focusing on delivering returns relative to the stock market. Early indications are encouraging, with the Fund returning 7.4% per year in Australian dollars after two years.

The Fund does not gear or use derivatives and will never have a share exposure of more than 50%. In certain market conditions (when the market is overvalued) the Fund may have no share exposure at all with all money invested in cash deposits.

Over time, the aim is to have higher share exposure when many shares in the market are trading at a discount to our estimate of intrinsic value (and thus yield investment opportunities that should give good absolute returns).

The Allan Gray and Orbis philosophy and approach remains the same, irrespective of geography

Although the opportunity set available in Australia is different from that of South African investments, Allan Gray Australia's investment philosophy and approach is the same as that of Allan Gray and Orbis. We focus on our discipline of assessing a company's true intrinsic value and we only invest when the share price that we will pay is substantially lower than the value we are buying to ensure that we have a margin of safety for each share in our portfolio.

Is Australia the right diversification opportunity for you?

While the differences between South Africa and Australia currently outweigh the similarities, in a global context, the diversification opportunity may not be appropriate for everyone. However, if you are planning to move to Australia, or have family ties or business interests in Australia, it is probably worthwhile exploring. It is crucial of course that your investment decisions meet a specific need in your portfolio. If you need help with diversification, or investing in general, we encourage you to speak to a professional independent financial adviser.

The Allan Gray Australia Equity and Opportunity Funds are both available via the Allan Gray Offshore Investment Platform and have been approved by the FSB for marketing to South African investors.

[1] Source: Credit Suisse Global Investment Returns Yearbook 2013

JD joined Allan Gray Australia in 2010 as head of retail after spending nine years with Allan Gray South Africa as director of Allan Gray Unit Trust Management Company. He holds a B Proc Degree (University of Pretoria) and is an admitted attorney and CFP in South Africa.

LJ joined Allan Gray South Africa in 2005. He is responsible for the distribution of the Allan Gray Australia funds in South Africa. He holds a B Com, MBA and is a CFP.

ANTHONY FARR

ALLAN GRAY ORBIS FOUNDATION UPDATE

When one considers the importance of entrepreneurship in driving job creation, South Africa's very low level of entrepreneurial activity partly explains why our country has such unacceptably high levels of unemployment. Anthony Farr discusses the Allan Gray Orbis Foundation's ongoing drive to improve the entrepreneurial pipeline by focusing on improving South African youths' perceptions of their own capabilities and the opportunities around them.

Despite the wave of interest and rhetoric around the importance of an entrepreneurial culture in South Africa, sadly the hard facts do not support this aspiration. In the latest Global Entrepreneurship Monitor 2012 Report, the largest annual entrepreneurship study in the world covering countries representing approximately 85% of the world's economy, the proportion of South African adults involved in early stage entrepreneurial activity dropped to 7.3% from 9.1% in 2011. This was the lowest of all 10 Sub-Saharan Africa countries participating in the study and is probably half the level our country requires.

Further investigation revealed that this poor outcome stems from a weak entrepreneurial pipeline. Focusing specifically on youth between the ages of 18 and 34, the pool of potential entrepreneurs is drawn from those individuals who have a combination of both perceiving that there are good opportunities and perceiving themselves to have entrepreneurial capabilities. In South Africa this proportion of potential entrepreneurs in the total youth population is 20%, a full two-thirds less than the Sub-Saharan average of 60%. When one considers the importance of entrepreneurship in driving job creation, these statistics start to explain why our country has such unacceptably high levels of unemployment. This pipeline approach gives us a clue as to where to begin addressing the problem. If we are able to shift our youths' perception of both their capability and the level of opportunity around them it would quickly improve the depth of the country's overall entrepreneurial pipeline. Opportunities exist here at least as much as elsewhere in Sub-Saharan Africa, therefore the *perception* of opportunity and both actual and perceived capability offer important levers with which to influence the entrepreneurial culture of the country at source.

Addressing these levers is a complex task and there are no single responses that will tackle this deficit. However, at the Allan Gray Orbis Foundation we have come to respect the importance of two ingredients that we see as having an important influence on both levers, namely grit and community.

A focus on grit and community

In his book 'How Children Succeed', Canadian author Paul Tough speaks about the seven character traits which are key to success. They are grit, curiosity, self-control, social intelligence, zest, optimism and gratitude. The most intriguing one on this list is an old concept with a new term, 'grit'. According to Wikipedia, grit is defined as 'perseverance and passion for long-term goals'. In the Foundation's context, we call it 'Courageous Commitment', which is one of the five pillars against which we select future Allan Gray

Candidate-Fellows and which is then developed further as part of the Fellowship journey. We define it as 'the courage and dedication to continue, realising that applying consistent commitment has a way of overcoming'. Interestingly, given its importance in the Fellowship process, an increasing number of studies are pointing towards this notion of grit as a far better predictor of future success than other dimensions such as IQ. This resilience and unwavering determination are also key to unlocking a different level of perception of one's capabilities, as well as growing the universe of potential opportunities that one feels able to pursue.

Secondly, a powerful community, particularly one inspired by a 'Spirit of Significance' (a second pillar of the Foundation), has a catalysing impact on the boundaries of possibility for those within the community. Such communities in their own right, and through their natural fostering of grit among those involved, start to move the levers of capability and opportunity perception.

"WE'VE ALL BEEN THROUGH THE FIRE. THE FOUNDATION... HAS FULFILLED THE ROLE OF THIS CONSTANT DRIVE THAT ENCOURAGES US TO PUSH BEYOND WHERE WE FELT COMFORTABLE." (ALLAN GRAY FELLOW)

The Foundation looks to accelerate the building of community through a number of avenues. In addition to online platforms and social media, the entire Fellowship cohort is brought together at the start of their journey at the 'Fellowship Connect' event. At Connect, second year Candidate-Fellows gather in Villiersdorp to make an impact on a cohort of Grade 9s at a local school by working to create a programme that instils a sense of belief and hope in these learners. This is part of a long-term project in which the concept of legacy is shared in an experiential manner and kick-starts the Candidate-Fellows Legacy Project. By utilising the mechanism of a shared experience, the power of the Fellowship community is cemented.

Association of Allan Gray Fellows

The Association of Allan Gray Fellows continues to gain momentum both in terms of growth and early stage entrepreneurial activity. At the end of 2012, 53 additional Allan Gray Fellows graduated, joining the existing 98 to make a total of 151 Alumni. An Allan Gray Fellow's initiative, The Eduvator Platform, which was begun during the annual Association Startership Challenge, received R50 000 from the Design Indaba and R25 000 from E². The concept involves a crowd-sourced funding platform that allows citizens to donate a small contribution, which is then used to make improvements to the classroom environments of underprivileged schools. Benefactors are able to observe the results of their contributions in real time, via a technological platform. The Association's executive team continues its efforts to ensure that the Association remains a focused body with strong ties to the Foundation and one which regularly participates in Foundation activities.

Allan Gray Fellowship

In its eighth year, the Foundation has 241 Candidate Allan Gray Fellows across nine campuses in South Africa. We proudly recognise some of the recent Fellow achievements:

- A Fellow was listed in the recent City Press publication '100 World Class South Africans'
- Out of the five national Rhodes Scholarships awarded last year, three were Fellows
- One Fellow was chosen as a Fulbright Scholar
- A Fellow was placed second in the World Debating Championship in Turkey
- A Fellow is the current UCT SRC President
- A Fellow was runner up in the television series selecting South Africa's One Day Leader

Fellowship selection for placement in 2014 is progressing well and in recognition of prior school performance in consistently producing Candidate Allan Gray Fellows, the latest listing of the Foundation's 100 Circle of Excellence Schools can be found by clicking on the 'Partners' tab in the 'About us' section of our website.

Allan Gray Scholarship

In its sixth year, the Foundation has 175 Allan Gray Scholars across 21 leading schools in South Africa. Since our update in Quarterly Commentary 4, 2012, we have completed the selection process for placement next year, resulting in 30 additional Allan Gray Scholarships being offered. We have celebrated the recent achievements of some of these Scholars including a head boy of Selborne College for the second year in a row, head girl of Rhenish High School, a deputy head boy of Bishops Diocesan College, selection for international exchange programmes, a top academic in grade and a gold medal in the Science Expo.

Improving the entrepreneurial pipeline

In conclusion, as we strive to improve the quality and depth of our own entrepreneurial pipeline, this combination of instilling grit within a focused community was best encapsulated at the recent Foundation Graduation where one of the Allan Gray Fellows had this to say:

'We've all been through the fire. The Foundation over the years has fulfilled the role of this constant drive that encouraged us to push beyond where we felt comfortable. We've seen each other stumble, we've poured out our hearts and, as a result, are privy to secrets very few others ever will be. It is this connection that has created a bond so strong that we cannot help but offer support when we see another Fellow trip; but at the same time, it is this same "bond" that causes us to revel in each other's successes. Fellows, today we celebrate, because today we see four years of effort, determination and drive carrying us over the finishing line.'

Second year Candidate-Fellows connect with scholars at the 'Fellowship Connect' event.

Allan Gray Orbis Foundation

Anthony is a qualified chartered accountant. Prior to joining the Allan Gray Orbis Foundation in 2005 he worked at the Starfish Greathearts Foundation.

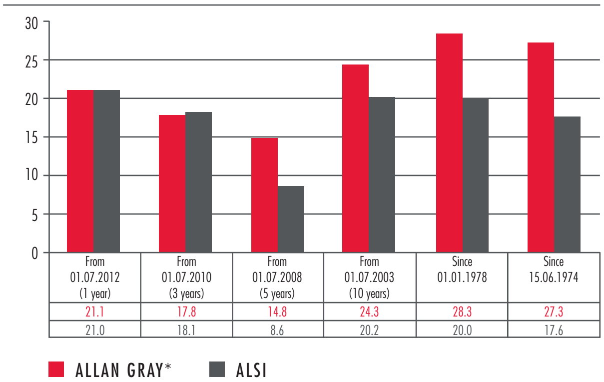
NOTES

INVESTMENT TRACK RECORD – SHARE RETURNS

ALLAN GRAY PROPRIETARY LIMITED GLOBAL MANDATE SHARE RETURNS VS JSE ALL SHARE INDEX

PERIOD	ALLAN GRAY*	JSE ALL SHARE INDEX	OUT/UNDER-PERFORMANCE
1974 (from 15.06)	-0.8	-0.8	0.0
1975	23.7	-18.9	42.6
1976	2.7	-10.9	13.6
1977	38.2	20.6	17.6
1978	36.9	37.2	-0.3
1979	86.9	94.4	-7.5
1980	53.7	40.9	12.8
1981	23.2	0.8	22.4
1982	34.0	38.4	-4.4
1983	41.0	14.4	26.6
1984	10.9	9.4	1.5
1985	59.2	42.0	17.2
1986	59.5	55.9	3.6
1987	9.1	-4.3	13.4
1988	36.2	14.8	21.4
1989	58.1	55.7	2.4
1990	4.5	-5.1	9.6
1991	30.0	31.1	-1.1
1992	-13.0	-2.0	-11.0
1993	57.5	54.7	2.8
1994	40.8	22.7	18.1
1995	16.2	8.8	7.4
1996	18.1	9.4	8.7
1997	-17.4	-4.5	-12.9
1998	1.5	-10.0	11.5
1999	122.4	61.4	61.0
2000	13.2	0.0	13.2
2001	38.1	29.3	8.8
2002	25.6	-8.1	33.7
2003	29.4	16.1	13.3
2004	31.8	25.4	6.4
2005	56.5	47.3	9.2
2006	49.7	41.2	8.5
2007	17.6	19.2	-1.6
2008	-12.6	-23.2	10.6
2009	28.8	32.1	-3.3
2010	20.9	19.0	1.9
2011	7.1	2.6	4.5
2012	20.6	26.7	-6.1
2013 (to 30.06)	6.7	2.3	4.4

RETURNS ANNUALISED TO 30.06.2013



* Allan Gray commenced managing pension funds on 1 January 1978. The returns prior to 1 January 1978 are of individuals managed by Allan Gray, and these returns exclude income. Returns are before fees.

Note: Listed property included from 1 July 2002.

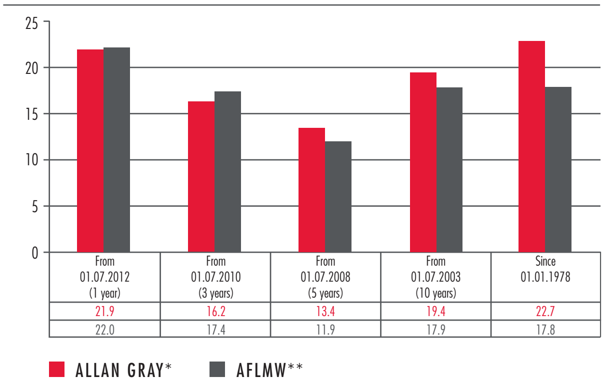
An investment of R10 000 made with Allan Gray on 15 June 1974 would have grown (before fees) to R122 591 871 by 30 June 2013. By comparison, the returns generated by the JSE All Share Index (before any fees) over the same period would have grown a similar investment to R5 645 485.

INVESTMENT TRACK RECORD – BALANCED RETURNS

ALLAN GRAY PROPRIETARY LIMITED GLOBAL MANDATE TOTAL RETURNS VS ALEXANDER FORBES GLOBAL MANAGER WATCH

PERIOD	ALLAN GRAY*	AFLMW**	OUT/UNDER-PERFORMANCE
1974	-	-	-
1975	-	-	-
1976	-	-	-
1977	-	-	-
1978	34.5	28.0	6.5
1979	40.4	35.7	4.7
1980	36.2	15.4	20.8
1981	15.7	9.5	6.2
1982	25.3	26.2	-0.9
1983	24.1	10.6	13.5
1984	9.9	6.3	3.6
1985	38.2	28.4	9.8
1986	40.3	39.9	0.4
1987	11.9	6.6	5.3
1988	22.7	19.4	3.3
1989	39.2	38.2	1.0
1990	11.6	8.0	3.6
1991	22.8	28.3	-5.5
1992	1.2	7.6	-6.4
1993	41.9	34.3	7.6
1994	27.5	18.8	8.7
1995	18.2	16.9	1.3
1996	13.5	10.3	3.2
1997	-1.8	9.5	-11.3
1998	6.9	-1.0	7.9
1999	80.0	46.8	33.1
2000	21.7	7.6	14.1
2001	44.0	23.5	20.5
2002	13.4	-3.6	17.1
2003	21.5	17.8	3.7
2004	21.8	28.1	-6.3
2005	40.0	31.9	8.1
2006	35.6	31.7	3.9
2007	14.5	15.1	-0.6
2008	-1.1	-12.3	11.2
2009	15.6	20.3	-4.7
2010	11.7	14.5	-2.8
2011	12.6	8.8	3.8
2012	15.1	20.0	-4.9
2013 (to 30.06)	11.5	8.7	2.8

RETURNS ANNUALISED TO 30.06.2013



** Consulting Actuaries Survey returns used up to December 1997. The return from 1 April 2010 is the average of the non-investable Alexander Forbes Large Manager Watch. The return for June 2013 is an estimate.

An investment of R10 000 made with Allan Gray on 1 January 1978 would have grown (before fees) to R14 153 563 by 30 June 2013. The average total performance (before fees) of global mandates of Large Managers over the same period would have grown a similar investment to R3 325 407.

ALLAN GRAY UNIT TRUSTS ANNUALISED PERFORMANCE IN PERCENTAGE PER ANNUM TO 30 JUNE 2013

UNIT TRUSTS[1]	QTR[3] (UNANNUALISED)	1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	ASSETS UNDER MANAGEMENT (R MILLION)	INCEPTION DATE
HIGH NET EQUITY EXPOSURE (100%)								
Allan Gray Equity Fund (AGEF)	-	**17.3**	**15.9**	**11.4**	**20.8**	**26.6**	33 145.4	01.10.98
FTSE/JSE All Share Index		21.0	18.1	8.6	20.2	18.3		
Allan Gray-Orbis Global Equity Feeder Fund (AGOE)	-	**62.1**	**25.5**	**11.9**	**-**	**14.8**	9 016.6	01.04.05
FTSE World Index (Rands)		44.2	24.1	8.4	-	12.1		
MEDIUM NET EQUITY EXPOSURE (40% - 75%)								
Allan Gray Balanced Fund (AGBF)	-	**20.1**	**14.9**	**12.0**	**18.0**	**19.5**	70 348.8	01.10.99
Average of South African - Multi Asset - High Equity category (excl. AGBF)[10]		18.9	14.4	9.9	15.7	13.9		
Allan Gray-Orbis Global Fund of Funds (AGGF)	-	**46.3**	**18.7**	**10.5**	**-**	**10.7**	9 385.2	03.02.04
60% of the FTSE World Index and 40% of the JP Morgan Government Bond Index Global (Rands)		32.3	19.6	9.0	-	10.0		
LOW NET EQUITY EXPOSURE (20% - 40%)								
Allan Gray Stable Fund (AGSF) - (Net of tax)	-	**12.9**	**9.3**	**9.3**	**11.6**	**12.5**	30 508.2	01.07.00
Call deposits plus two percentage points (Net of tax)		4.6	4.9	6.0	6.5	7.1		
Allan Gray Stable Fund (AGSF) - (Gross of tax)	-	**13.3**	**9.8**	**10.0**	**12.5**	**13.7**	30 508.2	01.07.00
Call deposits plus two percentage points (Gross of tax)		6.2	6.6	8.1	8.7	9.6		
VERY LOW NET EQUITY EXPOSURE (0% - 20%)								
Allan Gray Optimal Fund (AGOF)	-	**4.5**	**3.8**	**6.3**	**7.3**	**8.0**	905.8	01.10.02
Daily call rate of FirstRand Bank Ltd		4.1	4.5	6.0	6.6	7.0		
Allan Gray-Orbis Global Optimal Fund of Funds (AGOO)	-	**34.0**	**13.6**	**-**	**-**	**11.1**	721.2	02.03.10
Average of US$ Bank Deposits and Euro Bank deposits		24.0	11.1	-	-	8.3		
NO EQUITY EXPOSURE								
Allan Gray Bond Fund (AGBD)	-	**7.2**	**10.3**	**11.5**	**-**	**9.6**	773.9	01.10.04
BEASSA All Bond Index (total return)		6.3	10.7	12.2	-	9.3		
Allan Gray Money Market Fund (AGMF)	-	**5.2**	**5.7**	**7.3**	**7.9**	**8.5**	7 556.1	03.07.01
Alexander Forbes Short Term Fixed Interest (STeFI) Composite Index[9]		5.3	5.6	7.1	7.8	8.4		

ALLAN GRAY TOTAL EXPENSE RATIOS (TERS)

	EQUITY FUND	GLOBAL EQUITY FEEDER FUND	BALANCED FUND	GLOBAL FUND OF FUNDS	STABLE FUND	OPTIMAL FUND	GLOBAL OPTIMAL FUND OF FUNDS	BOND FUND	MONEY MARKET FUND
Performance component	0.72%	-0.22%	0.14%	-0.01%	0.43%	0.00%	0.01%	0.00%	0.00%
Fee at benchmark	1.71%	1.49%	1.17%	1.26%	1.13%	1.14%	0.98%	0.29%	0.29%
Total fees*	**2.43%**	**1.27%**	**1.31%**	**1.25%**	**1.56%**	**1.14%**	**0.99%**	**0.29%**	**0.29%**
Trading costs	0.05%	0.14%	0.07%	0.18%	0.06%	0.06%	0.18%	0.00%	0.00%
Other expenses	0.01%	0.06%	0.02%	0.08%	0.02%	0.01%	0.07%	0.02%	0.01%
TOTAL EXPENSE RATIO (TER)	2.49%	1.47%	1.40%	1.51%	1.64%	1.21%	1.24%	0.31%	0.30%
Annualised fee* rate for latest quarter	**2.70%**	**1.76%**	**2.15%**	**3.63%**	**2.51%**	**1.14%**	**4.94%**	**0.35%**	**0.29%**

* Including underlying Orbis Fund fees.

A Total Expense Ratio (TER) of a portfolio is a measure of the portfolio's assets that were relinquished as a payment of services rendered in the management of the portfolio. The total operating expenses are expressed as a percentage of the average value of the portfolio, calculated for the year to 31 March 2013. Included in the TER is the proportion of costs incurred by the performance component, fee at benchmark and other expenses. These are disclosed separately as percentages of the net asset value. Trading costs (including brokerage, VAT, STT, STRATE, levy and insider trading levy) are included in the TER. A high TER will not necessarily imply a poor return nor does a low TER imply a good return. The current TER cannot be regarded as an indication of future TERs.

ORBIS FUNDS ANNUALISED PERFORMANCE IN PERCENTAGE PER ANNUM TO 30 JUNE 2013

	QTR (UNANNUALISED)	1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	INCEPTION DATE
ORBIS FUNDS (RANDS) REGISTERED FOR MARKETING IN SOUTH AFRICA[1, 6]							
Orbis Global Equity Fund (Rands)	**15.7**	**61.5**	**25.5**	**11.9**	**14.5**	**18.9**	01.01.90
FTSE World Index (Rands)	8.1	43.4	23.7	8.2	11.3	12.8	
Orbis SICAV Japan Equity (Yen) Fund (Rands)	**14.1**	**50.1**	**23.0**	**12.5**	**12.1**	**15.2**	01.01.98
Tokyo Stock Price Index (Rands)	12.2	46.5	18.5	5.2	9.0	7.9	
Orbis SICAV Asia Ex-Japan Equity Fund (Rands)	**5.6**	**38.4**	**19.5**	**11.2**	**-**	**16.5**	01.01.06
MSCI Asia Ex-Japan (Rands)	2.2	32.2	15.3	8.6	-	14.3	
Orbis Optimal SA Fund-US$ Class (Rands)	**12.5**	**34.1**	**12.4**	**8.3**	**-**	**11.6**	01.01.05
US$ Bank Deposits (Rands)	7.9	21.6	9.2	5.4	-	9.1	
Orbis Optimal SA Fund-Euro Class (Rands)	**13.7**	**35.8**	**14.0**	**5.1**	**-**	**10.6**	01.01.05
Euro Bank Deposits (Rands)	9.2	24.3	11.9	1.9	-	8.3	

SEGREGATED AND LIFE POOLED PORTFOLIOS ANNUALISED PERFORMANCE IN PERCENTAGE PER ANNUM TO 30 JUNE 2013

	QTR (UNANNUALISED)	1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	ASSETS UNDER MANAGEMENT (R MILLION)	INCEPTION DATE
SEGREGATED PORTFOLIOS[5] (BEFORE FEES, EXCEPT FOR FUNDS INDICATED BY FOOTNOTE 1)								
Domestic Equity Composite FTSE/JSE All Share Index	**-1.0** -0.2	**19.8** 21.0	**17.3** 18.1	**13.7** 8.6	**24.0** 20.2	**21.7** 14.9	56 194.1	01.01.90
Domestic Balanced Composite Mean of Alexander Forbes Domestic Manager Watch[2,7]	**-1.1** 0.3	**13.9** 15.6	**14.0** 15.9	**13.2** 12.2	**20.5** 18.9	**23.0** 18.2	21 532.3	01.01.78
Global Balanced Composite Mean of Alexander Forbes Global Large Manager Watch[2,4]	**2.6** 2.5	**21.9** 22.0	**16.2** 17.4	**13.4** 11.9	**19.4** 17.9	**22.7** 17.8	45 151.9	01.01.78
Global Balanced Namibian High Foreign Composite Mean of Alexander Forbes Namibia Average Manager[2]	**3.8** 2.7	**24.3** 22.0	**16.2** 17.0	**12.8** 11.7	**18.9** 17.6	**19.7** 14.7	7 924.7	01.01.94
Foreign Best View (Rands) Composite[1,8] 60% of the MSCI and 40% of the JP Morgan Government Bond Index Global (Rands)	**13.5** 6.4	**45.8** 31.0	**18.4** 18.9	**10.2** 8.6	**11.5** 10.3	**14.9** 11.4	6 428.8	23.05.96
Relative Domestic Equity Composite Weighted average of client specific benchmarks[2]	**0.8** 0.7	**22.7** 20.8	**18.2** 18.7	**12.4** 10.6	**22.2** 20.6	**21.0** 16.3	4 805.3	19.04.00
LIFE POOLED PORTFOLIOS (BEFORE FEES, EXCEPT FOR FUNDS INDICATED BY FOOTNOTE 1)								
Domestic Equity Portfolio FTSE/JSE All Share Index	**-0.8** -0.2	**21.4** 21.0	**18.0** 18.1	**14.1** 8.6	**24.3** 20.2	**23.6** 16.0	7 364.1	01.02.01
Domestic Balanced Portfolio Mean of Alexander Forbes Domestic Manager Watch[2,7]	**-1.1** 0.3	**14.6** 15.6	**14.6** 15.9	**13.5** 12.2	**20.9** 18.9	**20.2** 16.8	6 677.2	01.09.01
Global Balanced Portfolio Mean of Alexander Forbes Global Large Manager Watch[2,7]	**2.7** 2.5	**22.4** 22.0	**16.5** 17.4	**13.7** 11.9	**19.5** 17.9	**20.2** 15.4	25 054.9	01.09.00
Domestic Stable Portfolio Alexander Forbes Three-Month Deposit Index plus 2%	**0.4** 1.7	**6.9** 7.2	**8.0** 7.6	**10.4** 9.0	**14.3** 9.8	**14.6** 10.5	1 974.7	01.12.01
Global Stable Portfolio Alexander Forbes Three-Month Deposit Index plus 2%	**3.4** 1.7	**14.7** 7.2	**10.9** 7.6	**10.8** 9.0	**-** -	**14.0** 9.7	4 016.1	15.07.04
Domestic Absolute Portfolio Mean of Alexander Forbes Domestic Manager Watch[7]	**-0.8** 0.3	**5.5** 15.6	**8.4** 15.9	**12.1** 12.2	**19.7** 18.9	**21.3** 16.5	1 062.5	06.07.01
Global Absolute Portfolio Mean of Alexander Forbes Global Large Manager Watch[2,7]	**2.3** 2.5	**13.8** 22.0	**11.2** 17.4	**12.6** 11.9	**-** -	**18.0** 16.8	3 400.9	01.03.04
Orbis Global Equity Portfolio[1] FTSE World Index (Rands)	**15.8** 8.1	**61.2** 43.4	**25.2** 23.7	**12.0** 8.2	**-** -	**14.4** 11.8	5 192.3	18.05.04
Foreign Portfolio[1] 60% of the MSCI Index and 40% JP Morgan Government Bond Index Global (Rands)	**13.3** 6.4	**45.4** 31.0	**18.1** 18.9	**10.0** 8.6	**11.5** 10.3	**7.7** 5.3	1 479.4	23.01.02
Hedged Domestic Equity Portfolio FTSE/JSE CAPI Index	**-0.9** -0.1	**18.6** 21.3	**16.5** 18.3	**13.6** 9.9	**-** -	**11.5** 8.5	1 089.9	01.06.08
Relative Domestic Equity Portfolio FTSE/JSE CAPI Index	**0.1** -0.1	**22.3** 21.3	**17.0** 18.3	**11.1** 9.9	**21.9** 20.7	**22.7** 21.5	237.1	05.05.03
Domestic Optimal Portfolio[1] Daily Call Rate of Nedcor Bank Limited	**1.0** 1.1	**5.3** 4.4	**4.6** 4.8	**7.4** 6.2	**8.2** 6.9	**8.4** 7.2	352.3	04.12.02
Domestic Medical Scheme Portfolio Consumer Price Index plus 3% p.a.[2]	**0.1** 0.6	**6.7** 8.1	**8.0** 8.3	**10.1** 8.4	**-** -	**13.1** 9.0	1 487.2	01.05.04
Money Market Portfolio[1] Alexander Forbes Three-Month Deposit Index	**1.3** 1.2	**5.4** 5.1	**5.9** 5.5	**7.5** 6.9	**8.2** 7.7	**8.9** 8.5	330.4	21.09.00

PERFORMANCE AS CALCULATED BY ALLAN GRAY

1 The fund returns are net of investment management fees
2 The return for the quarter ending 30 June 2013 is an estimate as the relevant survey results have not yet been released
3 Unable to disclose due to ASISA regulations
4 Consulting Actuaries Survey returns used to 31 December 1997. Alexander Forbes Global Large Manager Watch used from 1 January 1998. Alexander Forbes Non-Investable Large Manager Watch used from 1 April 2010
5 The composite assets under management figures shown include the assets invested in the pooled portfolios above where appropriate
6 Amounts invested by the Allan Gray client portfolios in the Orbis funds are included in the assets under management figures in the table above
7 The mean returns of the Alexander Forbes Non-Investable Large Manager Watch used from 1 April 2010
8 The foreign carve-out returns of the Global Balanced Composite used from 23 May 1996 to 31 August 2001. The Foreign Balanced Composite returns are used from 1 September 2001
9 Alexander Forbes Three-Month Deposit Index from 3 July 2001 to 31 March 2003. As from 1 April 2003, the benchmarck is the simple average of the Domestic Fixed Interest Money Market Unit Trust Sector excluding the Allan Gray Money Market Fund. The benchmark from 1 November 2011 is the Alexander Forbes Short Term Fixed Interest (STeFI) Composite Index
10 The benchmark was the daily weighted average of the Domestic Prudential Medium Equity Unit Trust sector excluding Allan Gray Balanced Fund from inception until 31 December 2007. With effect from 1 January 2008 it was changed to the daily weighted average (based on assets under management) of the Domestic Prudential Medium Equity Unit Trust Sector and the Prudential Variable Equity Sector excluding Allan Gray Balanced Fund. The change was as a result of the Allan Gray Balanced Fund being reclassified from the Domestic Prudential Medium Equity Sector to the new Prudential Variable Equity Sector. The benchmark from 1 February 2013 is the daily weighted average return of funds in the South African - Multi Asset - High Equity category (excluding the Allan Gray Balanced Fund)

ALLAN GRAY BALANCED AND STABLE FUND ASSET ALLOCATION AS AT 30 JUNE 2013

	BALANCED FUND % OF PORTFOLIO			STABLE FUND % OF PORTFOLIO		
	TOTAL	SA	FOREIGN**	TOTAL	SA	FOREIGN
Net equitites	55.7	41.9	13.8	15.2	10.5	4.7
Hedged equities	15.4	2.5	12.8	36.4	16.3	20.1
Property	0.8	0.6	0.2	0.4	0.2	0.2
Commodities	2.8	2.8	0.0	3.4	3.4	0.0
Bonds	9.5	9.4	0.1	4.4	4.4	0.0
Money market and bank deposits	15.8	13.2	2.7	40.2	36.9	3.3
TOTAL	**100.0**	**70.4**	**29.6***	**100.0**	**71.8**	**28.2***

Note: There might be slight discrepancies in the totals due to rounding.

* The Fund is above its foreign exposure limit due to market value movements.
** This includes African ex-SA assets.

ALLAN GRAY EQUITY FUND NET ASSETS AS AT 30 JUNE 2013

SECURITY (RANKED BY SECTOR)	MARKET VALUE (R MILLION)	% OF FUND	JSE ALSI WEIGHT (%)
EQUITIES	**32 538**	**98.2**	
RESOURCES	**8 079**	**24.4**	**25.8**
Sasol	3 772	11.4	
Anglo American[1]	1 336	4.0	
BHP Billiton	890	2.7	
Impala Platinum	517	1.6	
Anglogold Ashanti	431	1.3	
Positions less than 1%	1 133	3.4	
FINANCIALS	**8 328**	**25.1**	**20.5**
Standard Bank	1 802	5.4	
Reinet Investments SA	1 323	4.0	
Sanlam	1 224	3.7	
Investec	1 000	3.0	
Old Mutual	996	3.0	
Rand Merchant Insurance	343	1.0	
Positions less than 1%	1 641	5.0	
INDUSTRIALS	**15 875**	**47.9**	**53.7**
British American Tobacco	3 840	11.6	
SABMiller	2 899	8.8	
Remgro	2 104	6.4	
Netcare	635	1.9	
Mondi	545	1.6	
Nampak	527	1.6	
Tongaat-Hulett	518	1.6	
Naspers	456	1.4	
Sappi	405	1.2	
Datatec	386	1.2	
Illovo Sugar	347	1.1	
Positions less than 1%	3 213	9.7	
OTHER SECURITIES	**256**	**0.8**	
MONEY MARKET AND CALL DEPOSITS	**608**	**1.8**	
TOTALS	**33 145**	**100.0**	

[1] Including positions in Anglo American stub certificates.

THE ALLAN GRAY GROUP	
UNIT TRUSTS	A unit trust is a savings vehicle for investors who want to grow their money and may want to access it before they retire. Unit trusts allow investors to pool their money with other investors who have similar investment objectives. Unit trusts are also known as 'portfolios of collective investment schemes' or 'funds'. Allan Gray has nine funds in its stable: Equity, Balanced, Stable, Optimal, Money Market, Bond, Global Equity Feeder, Global Fund of Funds and Global Optimal Fund of Funds.
RETIREMENT ANNUITY*	The Allan Gray Retirement Annuity Fund (RA) is a savings vehicle for investors looking for a flexible, tax-efficient way to save for retirement. Investors can only access their money when they retire. Individually owned RAs can be managed on a group basis, offering employers a flexible solution to the challenge of retirement funding for their staff.
PRESERVATION FUNDS*	The Allan Gray Pension Preservation and Provident Preservation funds are savings vehicles for investors looking for a tax-efficient way to preserve existing retirement benefits when they leave a pension or provident fund, either as a result of a change in employment (e.g. retrenchment or resignation), or when they transfer from another preservation fund.
ENDOWMENT*	The Allan Gray Endowment Policy is a savings policy for investors who want a tax-efficient way to save, and wish to create liquidity in their estate.
LIVING ANNUITY*	The Allan Gray Living Annuity gives investors flexibility, within certain regulatory limits, to select an annuity best suited to their income needs after retirement. A living annuity provides investors with a regular income which is not guaranteed, and which is funded by growth on capital and income from interest and dividends.
OFFSHORE FUNDS	Through our partnership with Orbis we offer you a cost-effective way to diversify your portfolio by investing offshore. There are two options for investing offshore through Allan Gray: invest in rand-denominated offshore funds without the need to use your offshore investment allowance, or use your offshore investment allowance to invest in foreign funds.
PLATFORM – LOCAL AND OFFSHORE	Our investment platform provides you with access to all of our products, as well as a focused range of unit trusts from other fund providers. The platform enables you to buy, sell and switch – usually at no charge – between the funds as your needs and objectives change. South African investors who wish to diversify their portfolios can also access funds from certain other offshore fund providers via the same platform.
LIFE POOLED PORTFOLIOS	The minimum investment per client is R20 million. Mandates include risk-profiled pooled portfolios: Stable Portfolio, Balanced Portfolio and Absolute Portfolio; asset class pooled portfolios: Money Market, Equity and Foreign, and finally an Optimal Portfolio. Institutional investments are currently restricted to existing investors only (except for foreign mandates).
SEGREGATED PORTFOLIOS	The minimum portfolio size is R500 million. Mandates are of a balanced or asset class specific nature. Portfolios can be managed on an absolute or relative risk basis. Institutional investments are currently restricted to existing investors only (except for foreign mandates).
BOTSWANA	Allan Gray Botswana manages institutional portfolios on a segregated basis, and offers our range of nine South African unit trusts to individual investors.
NAMIBIA	Allan Gray Namibia manages institutional portfolios on a segregated basis and the Allan Gray Namibia Investment Trust provides investment management for Namibian retirement funds in a pooled vehicle.
SWAZILAND	Allan Gray Swaziland manages institutional portfolios on a segregated basis.
ALLAN GRAY ORBIS FOUNDATION	Allan Gray Orbis Foundation is a non-profit organisation that was established in 2005 as an education and development catalyst. It seeks to foster a next generation of high-impact leaders and entrepreneurs for the ultimate purpose of increased job creation in Southern Africa. The Foundation focuses on educational and experiential methods at the secondary and tertiary levels to realise the potential of bright young minds. Through its highly researched learning programmes, it intends equipping talented young individuals with the skills, attitudes and motivation to have significant future impact.
E^2	E^2 stands for 'excellence in entrepreneurship' and as a long-term capital fund its purpose is to provide substantial financing to entrepreneurs who are graduates of the Allan Gray Fellowship Programme. In addition, E^2 provides financing for social entrepreneurs who demonstrate exceptional leadership and creative initiative in the not-for-profit sectors.

* This product has unit trusts as its underlying investment option.

Directors

M Cooper B Bus Sc FIA FASSA
RW Dower BSc (Eng) MBA
WB Gray B Com MBA CFA (Irish) (Non-Executive)
IS Liddle B Bus Sc (Hons) CFA
TJ Mahuma BA (Hons) MPhil (Non-Executive)
SC Marais PhD CFA (Non-Executive)
T Mhlambiso AB MBA JD
KC Morolo BSc (Eng) MEng (Non-Executive)

Company Secretary

CE Solomon B Bus Sc (Hons) CA (SA)

Registration Number

2005/002576/07

Business Address

Granger Bay Court Beach Road V&A Waterfront Cape Town 8001
P O Box 51318 V&A Waterfront Cape Town 8002 South Africa
Tel +27 (0)21 415 2300 Fax +27 (0)21 415 2400

www.allangray.co.za info@allangray.co.za

Client Service Centre

0860 000 654 / +27 (0)21 415 2301
Client Service Email info@allangray.co.za
Client / IFA Service Facsimile
0860 000 655 / +27 (0)21 415 2492
IFA Service Centre 0860 000 653
IFA Service Email ifa@allangray.co.za
Portswood Square Dock Road V&A Waterfront Cape Town 8001
