


The triumph of markets

Another view

Understanding the return of a fund

Development of the tele-communications profit pool

Q4

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QUARTERLY
COMMENTARY

Allan Gray

Rob Dower

COMMENTS FROM THE CHIEF OPERATING OFFICER

When I returned to South Africa from London with my young family in the early part of the last decade, we thought we were trading economic security for a warmer climate and the chance to raise our children around the corner from their grandparents. Looking back, there was no such trade-off. London was one of the riskier places to have invested your savings or to have spent time building a professional career in the last decade. And South Africa one of the safer places, at least economically. In common with many other emerging markets, South Africa has enjoyed a steady pace of growth and strong capital markets driven by a re-rating by global investors. To quote my colleague Ian Liddle, South Africa has been 'the place to be' in the last decade from an investment perspective.

Our firm is full of committed South Africans. We have ended the decade, however, on what we consider to be overly optimistic market valuations, given where we are in the economic cycle. The price/earnings (P/E) multiple on both local and global stock markets demands a recovery in earnings that seems to us to be unrealistic, especially since current JSE earnings remain above their long-term trend line. And our fiscus is in for a bruising as we borrow from future generations to fund massive (and overdue) infrastructure investment.

The 90s was a tough decade for our country and some of our success in the last 10 years can be attributed to reaping the benefits of earlier sacrifices. But some of the good times will also have to be paid for in the next decade. The paradox of markets is that valuations at the end of 1999 should have been optimistic and, we think, those at the end of 2009 pessimistic, not the other way round.

The financial crisis

Long-standing clients will know that this firm encourages diversity of opinion. In this issue, Sandy McGregor can see positive signs in the aftermath of the 2008 crisis, while Duncan Artus is a convincing bear.

Sandy points out that, while it is popular to claim the markets have failed investors over the past two years, the errors of individual bankers, economists and politicians do not constitute market failure. He explains how, over the last two years, market forces have imposed necessary adjustments which the political system would never have done. This is not a failure but a 'triumph' of the markets, and the world economy is now building foundations for the next up cycle.

However, there is some doubt about whether the global programmes of fiscal and monetary stimulus will improve the real economy sustainably, and it is unclear what effect the stimuli will have on equity valuations. Duncan Artus questions whether investors are being compensated sufficiently for the uncertainty of the success of the stimuli and the potential side-effects on capital markets.

As Jonathan Brodie and Trevor Black of our global partner Orbis discussed in the Q2 2009 Quarterly Commentary, investor success in the market depends on both investor and manager behaviour. This quarter the pair turn the spotlight on money manager behaviour over time. This is a well-timed piece as Orbis' flagship Global Equity Fund (US$) recently celebrated its 20th birthday, having achieved average growth of 13% over the last 20 years, versus its benchmark's 6.2%.

Look to the long term

The principles surrounding the growth of financial or human capital have a lot in common, and both benefit from a long-term strategy, as Anthony Farr discusses in the Allan Gray Orbis Foundation update.

Finally, thank you sincerely for your support over the last 10 years. You have our commitment to making the next decade a prosperous one, and we wish you well for the new year.

Kind regards

Rob Dower

Sandy McGregor

THE TRIUMPH OF MARKETS

EXECUTIVE SUMMARY: It is the nature of markets to reward success and eliminate what is unsustainable. During the past year we have seen a dramatic manifestation of this process, which has created the conditions necessary for renewed global growth. Although many people claim markets have failed, what has happened is actually a triumph of markets, which has forced changes that the political system would never have made.

It was a communist article of faith that ultimately capitalism would destroy itself. Accordingly, during the 1920s, the Communist Party of the Soviet Union commissioned the economist Nicolai Dmitriyevich Kondratieff to advise when this would happen. After giving the matter much thought, Kondratieff came up with two conclusions. Firstly, capitalism would not end or collapse. Market-based economies have an astonishing ability to reinvent themselves and to emerge resiliently from economic crises. Secondly, there is a market cycle of about 55 years. On the basis of this cycle, he predicted the travails that would follow 1929. Why 55 years? Kondratieff did not offer an explanation, but his work points to the probable answer. Fifty-five years represents two generations. People do learn from their mistakes, but not from history. Their behaviour changes with personal experience. A new generation with different experiences tends to repeat the mistakes of the past.

"People do learn from their mistakes, but not from history."

Kondratieff did not find favour with his Soviet masters. The Great Soviet Encyclopaedia restricted mention of him to one sentence: 'This economist was reactionary and wrong'. He was exiled to a labour camp in 1932 where writer and future Nobel Prize winner Alexandr Solzhenitsyn once had a fleeting sighting of him. Kondratieff was executed in 1938. However, his insights remain valuable and very relevant to our current economic situation.

Have markets failed?

It is commonplace to read, and hear comment on the financial crisis which has unfolded over the past two years, that the market economy has failed. British Prime Minister Gordon Brown has said that markets are discredited. The reality is somewhat different. Indeed, many individuals have been made to look very foolish. 'How did economists get it so wrong?' was the title of an article written by Nobel Prize winner Paul Krugman. Again this is nothing new. In 1300 Dante consigned the equivalent of errant economists, whom he called soothsayers who make false prophesies, to the lowest circle of hell. However, errors by individual bankers, economists and politicians do not mean markets are wrong. Over time markets, which are the aggregation of human behaviour, expunge error in a Darwinian process which rewards success and eliminates what is unsustainable.

Prior to 2007 a set of unsustainable imbalances was developing on an astonishing scale. They included:

- Property bubbles financed by reckless borrowing
- Reckless lending by banks
- An almost total absence of saving in many countries, including the United States
- Massive trade imbalances and an Asian growth model based on exports
- An overheated global economy forcing commodity prices up

It was apparent that we were on a path which could not last. The uncertainty was how we would get off it. Many market participants believed that somehow we would muddle through without too much suffering. However that was not to be. Market forces acted with a vengeance and astonishing rapidity. As a result the behaviour of individuals and institutions has changed dramatically. Within two years:

- The private savings rate is up strongly and, in all probability, the baby boom generation will remain significant savers. The shock of what has happened has fundamentally changed the way people regard the future and is creating a savings culture.
- Irresponsible lending and imprudent borrowing have practically ceased. There is much talk of the need to regulate banks to ensure that the bad practices, which contributed so massively to the debacle, are not repeated. In reality, the experience of the past two years has so changed behaviour that it will not be necessary to regulate bankers for a generation.
- Asian countries are increasingly redirecting their economies to domestic rather than export-driven growth.
- The shortage of commodities has eased significantly.

The triumph of markets

Recessions are an essential part of the process of economic growth. To a large extent, growth is synonymous with rising productivity and efficiencies. During long periods of prosperity inefficiencies and bad practices accumulate. In a recession these are eliminated, or at least reduced, and a platform is created for the next expansionary wave. What we have experienced recently is therefore not a failure but a triumph of the markets. Within two years market forces have imposed necessary adjustments and changes in behaviour which the political system would never have done. Much of what was unsustainable has been eliminated and the world economy is now building foundations for the next up cycle.

As world trade and the financial system imploded after Lehman's collapse, many commentators sought parallels with what happened in the 1930s. This is a misreading of history. The present recession has far more in common with the downturns of 1975 and 1982.

The recent recovery of markets has followed a path similar to what happened in those two years. It is encouraging that 1976 and 1983 witnessed strong growth, which gives confidence about the prospects for 2010. One intriguing parallel with 1975 is the sense of shock that the financial collapse caused. Between 1948 and 1974 the world experienced a continuing boom with relatively minor recessions. So events of 1975 took everyone by surprise. The same thing happened in 2008 when a generation of businessmen and investors had been lulled into complacency by what has come to be called the Great Moderation – 25 years during which markets were increasingly stable and benign. In both cases, the lessons of history were forgotten.

The political response to one crisis may create another

While the world's economy is recovering we still face considerable dangers, partly due to what may be unintended consequences of governments' reactions to the crisis. Political systems do not readily accept the harsh judgement of markets. Too many people have been hurt in what has been the most severe downturn since 1982. The response has been to slash interest rates and to print money in the hope that this will alleviate the pain. While this has proved to be a short-term panacea there will be longer-term costs. In effect, governments are trying to prevent the adjustments required by market forces. Those economists who advocate money creation as the solution to our current economic problems have much in common with a French minister of agriculture in the 1930s who, in order to increase the sale of wine, advocated wine as a cure for alcoholism. Money creation is like a drug, a difficult habit to break. Newly printed money is finding its way into asset prices. There is the danger that, in their response to the consequences of one asset bubble, governments are going to create another. If there is another bubble, it is a certainty that market forces will again take their toll.

Duncan Artus

ANOTHER VIEW

EXECUTIVE SUMMARY: Governments around the world are engaged in significant fiscal and monetary stimulus. But there is some doubt about whether their efforts will improve the real economy sustainably, and it is unclear what effect they will have on equity valuations. The question is, are investors being sufficiently compensated for the uncertainty of the success of the stimuli and for their potential side-effects on capital markets? If more debt and more spending are needed to support current price levels, it stands to reason also that, unless all of the cumulative spending and debt to date can be re-paid and/or rolled over, asset prices will have to fall.

'What is prudence in the conduct of every private family can scarce be folly in that of a great kingdom.' - Adam Smith

'An economy depends on the player's confidence. If confidence has been shaken by too much bad debt, restore confidence by adding more.' - Hunter Lewis

Regular readers of our recent commentaries will need little reminding that we have been cautious about the prospects for future real returns. A review of recent news, company results and investor comments leaves one with the impression that a significant portion of what is currently assumed in equity prices is based on the expected success of the current global fiscal (government spending) and monetary (low interest rates and quantitative easing) stimulus.

"Over long periods, overvalued assets tend to move back to fair value."

Debt is never free

Is excessive spending truly the way to long-term wealth? Is it better to incur debt than to save? I am certainly no economist but it does not make sense to me. Yet this is precisely what governments, central banks and many mainstream economists are advocating, and the 'easy money' argument is one of the cornerstones of the bullish argument for equities. The ultimate free lunch, if you will.

Expanding credit is a more pleasant way of saying that debt is expanding. If more debt and more spending across the globe are what is needed to support current asset prices (take a read through your daily newspaper), it follows that, unless this debt can be re-paid and/or rolled over at current levels, asset prices will have to fall. Debt has to be paid back, and if it cannot be repaid, it is defaulted on.

Default normally results from either purchasing overvalued assets with debt, or being unable to rollover the debt due to a lack of confidence among lenders, or a combination of both. Asset prices driven by leverage are invariably written down to more realistic levels and/or levels that holders of liquidity able to refinance the debt are willing to accept as collateral.

While this is a familiar, if painful chain of events for individuals with, for example, a mortgage or a business with too much debt, government debt also has to be serviced and eventually dealt with by either:

- Increasing the tax burden on citizens and businesses to repay the debt,
- Inflating the debt away via inflationist policies, that is, repaying the debt eventually with money that is worth much less than what was borrowed, or
- By defaulting.

Regardless of where the pain is borne, none of the above options would seem positive for the real value of businesses. Even now, sound businesses and prudent individuals who were cautious are being rewarded for that prudence by subsidising those who over-levered and over-expanded through direct subsidies (think 'Cash for Clunkers' – the US Car Allowance Rebate System), higher taxes and low yields on cash.

GRAPH 1 Net foreign investment into South African equities

Source: I-Net Bridge

'The profit system is effectively a profit and loss system. The stick of loss and bankruptcy is arguably more important than the carrot of profit in motivating the players and regulating the system. But Keynesianism rejects loss and bankruptcy as an unnecessary anachronism. Recessions are, if possible, avoided and, if not, papered over with bailouts and artificial stimulus. As a result, the errors of the past are never liquidated and new errors are piled atop the old.' - Hunter Lewis: Where Keynes went wrong.

The effect of easy money on short- and long-term asset prices

Other than perhaps in China, lending by banks continues to decline or grow very slowly despite the monetary and fiscal stimulus. So where has all the 'easy money' gone? It appears that much of it has gone into asset prices. This investment strategy works, until investors try to exit the trend simultaneously. Witness the net foreign outflows in the second half of 2008 in **Graph 1** as an example. (Of course everyone thinks they will be able to jump off first before any sell-off begins.)

Doubts over the sustainability of the trend may arise as the effect of the stimuli on the real economy and on fundamental equity valuations is unclear. The following graphs are two examples of this. **Graph 2** on page 6 shows the number of jobs in the US over the last 10 years, which contained two of the largest monetary stimuli in history. No net jobs have been created. **Graph 3** on page 6 shows the long and grinding decline in the Japanese Topix Index post the 1990 high despite the massive fiscal spending by the Japanese government over much of the next 20 years. Over long periods, overvalued assets tend to move back to fair value.

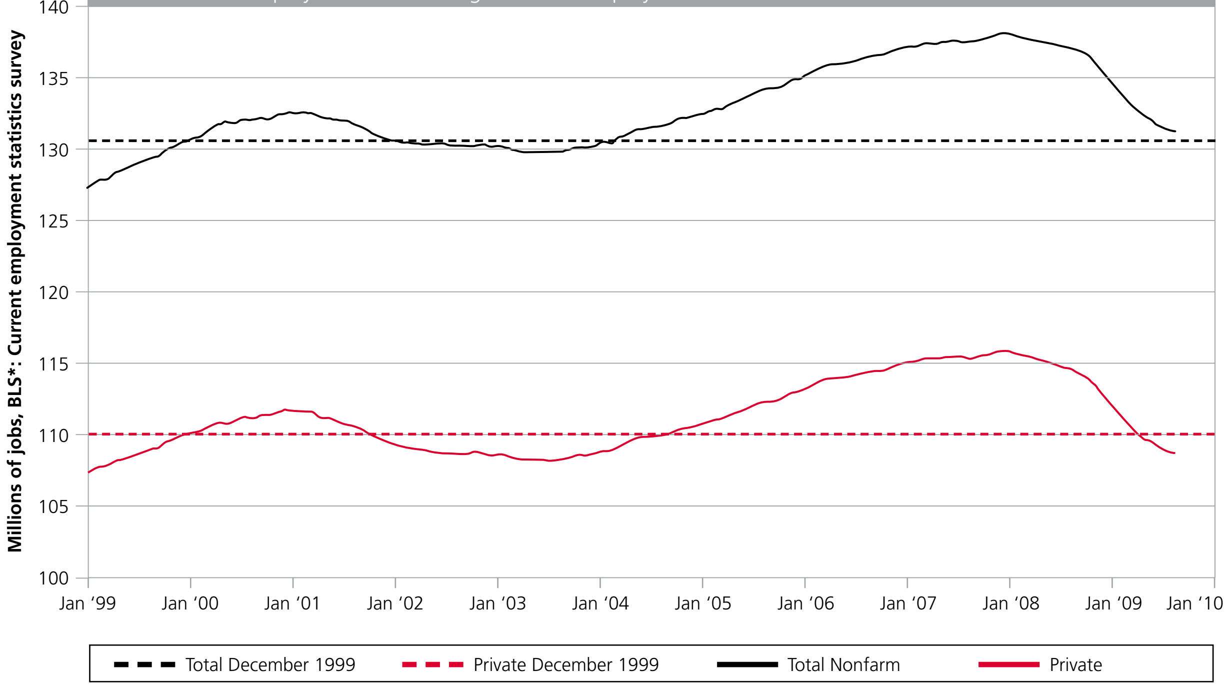
What are the implications of all this for investment strategy?

If there is some doubt about whether the fiscal and monetary stimuli will improve the real economy sustainably and justify a higher fair value for equities, the question is how much are investors being asked to pay for the assumed success of the stimulus? A lot, in my opinion.

The price/earnings (P/E) multiple of the FTSE/JSE All Share Index (ALSI) at 16.8x is well above its long-term average of 11.5x. The dividend yield of the ALSI at 2.25%, is half its long-term average of 4.5%. The sustainability of the current P/E and dividend yield are reliant on future earnings. The earnings of the market remain above the long-term trend.

There is, in my view, neither a significant margin of safety, nor is there significant upside in local equities. We have thus continued to reduce the exposure to equities in our asset allocation funds. The market could well continue to test our patience, as well as that of some of our clients, but hopefully we will be well rewarded with an opportunity to buy cheap assets.

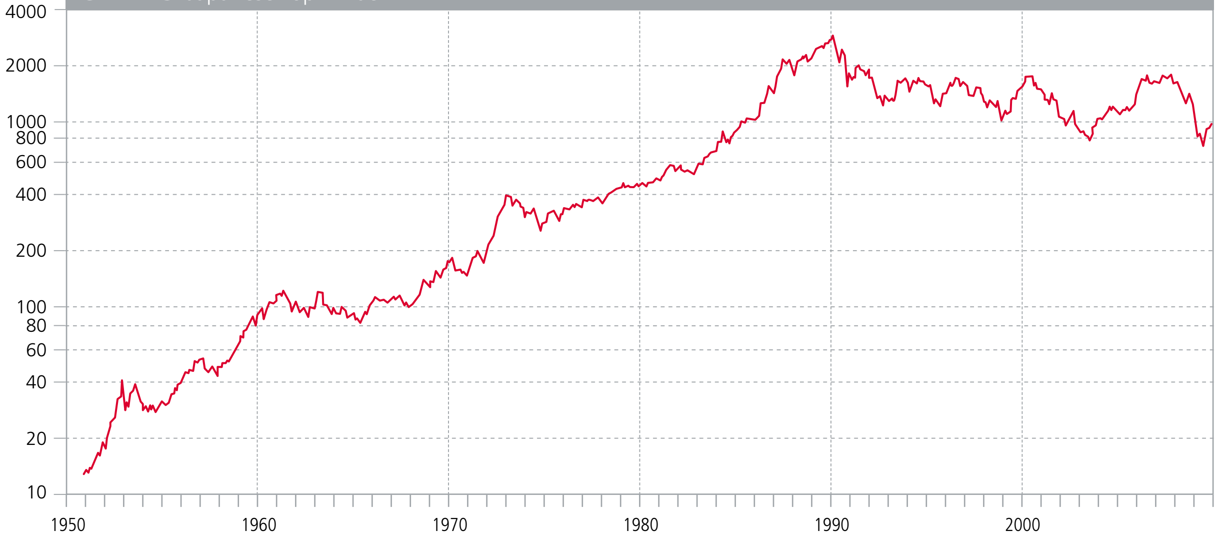
GRAPH 2 US employment in the naughts: a lost employment decade



Source: Bianco Research LLC

* US Bureau of Labour Statistics

GRAPH 3 Japanese Topix Index



Source: Thomson Reuters Datastream

Jan Silvis

DEVELOPMENT OF THE TELECOMMUNICATIONS PROFIT POOL

EXECUTIVE SUMMARY: The South African telecommunications profit pool has grown rapidly since the commercialisation of Telkom in the early 1990s. However, our analysis suggests that growth in the profit pool is under pressure and that the risks to forecasting future free cash flows have increased. The industry is also currently attracting record levels of new capital investment and returns on those investments are likely to be lower than those achieved in the past. Jan Silvis elaborates.

Historical perspective

The South African telecommunications market has grown rapidly since the early 1990s. In 1993 Telkom, then predominantly a fixed-line voice provider, converted from a government department to a commercial business. Around the same time, the South African mobile voice industry was born with the establishment of Vodacom and MTN.

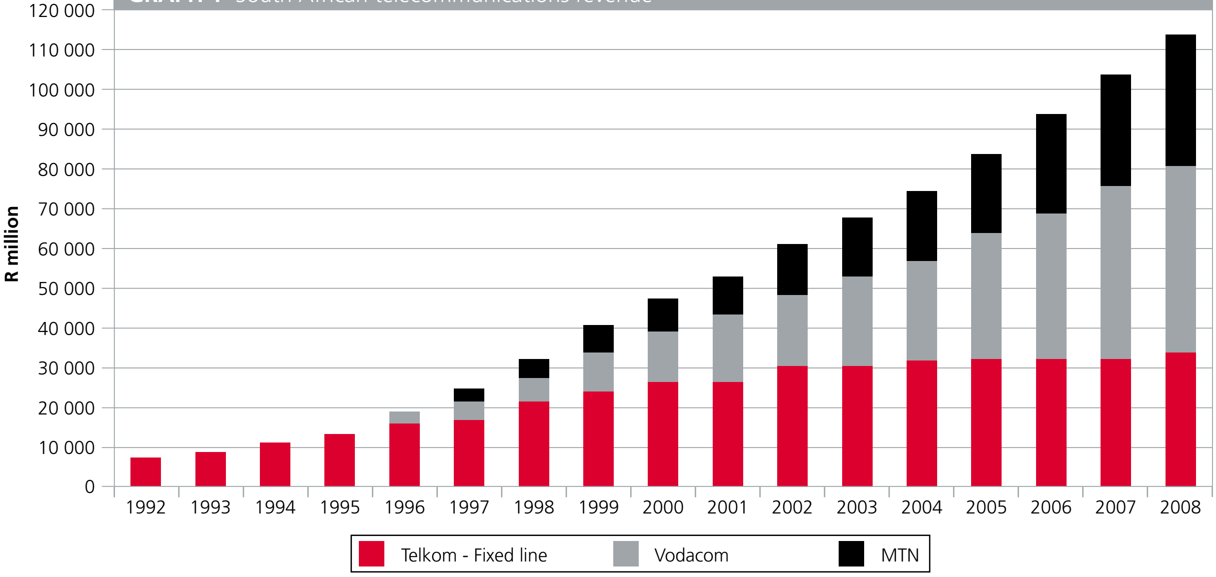
Today South Africa's business and private telecommunication needs are met by a large number of telecommunication infrastructure and service providers. Over time their offering has broadened to include a range of products such as fixed-line voice and data, mobile voice and data, and value-added services.

Industry revenue pool

One of the factors we consider when valuing individual companies is the underlying growth trend of the broader industry. **Graph 1** presents the South African reported revenue history for the three large listed operators as a proxy for the local telecommunications industry.

Reported revenue is up 16 times in 16 years and, on a combined basis, these three operators have shown a stable compound revenue growth rate of 19.0% per year. This secular increase in revenue has comfortably outpaced inflation of 6.8% per year over the same period and is mainly indicative of the value that mobile communication has created for society.

GRAPH 1 South African telecommunications revenue



Source: Company reports and Allan Gray research (Telkom/Vodacom lagged three months)

It is tempting to believe that this high and stable historical growth trend in reported industry revenue will persist and thus continue to support the investment case for most telecommunication companies in South Africa. However, our analysis indicates such a simplistic conclusion is inappropriate. No industry can maintain revenue growth in excess of nominal GDP over the very long term. After an extended period of high growth we would argue that the risks are to the downside.

Industry profit pool

As investors, we are more interested in a company's free cash flow than its revenue. It is therefore more relevant for us to examine the trend in operating profit, rather than reported revenue. **Graph 2** tracks the development of the telecommunication industry profit pool over time. This proxy for industry profits aggregates the unadjusted operating profits before interest and tax for the three large listed operators. **Graph 3** illustrates the same information adjusted for the effects of inflation.

Profits have been increasing dramatically as telecommunication companies capture some of the value they create for society. Operating profits are up 13.3 times in nominal and 4.6 times in real terms. Put differently, industry profits have grown at the exceptional compound annual rate of 17.5% in nominal and 10.1% in real terms. However, closer inspection of the profit pool development over time highlights three interesting observations which inform our future expectations:

1. Revenue growth does not equal operating profit growth

Growth in industry profits has not kept up with growth in industry revenues. One of the reasons for this observation is the way in which operators disclose reported revenues and costs.

At individual operator level, each operator includes revenue (cash inflow) from two sources in its reported revenue:

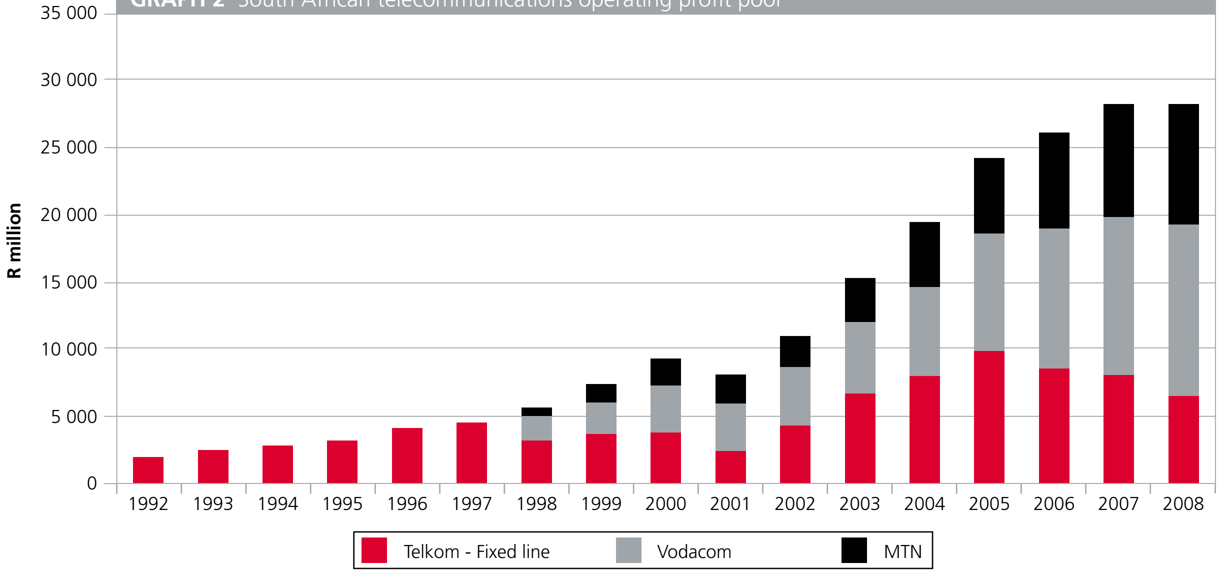
- Business and retail subscribers i.e. external subscriber revenue
- Other telecommunication operators connecting to their network to reach their subscribers i.e. interconnect revenue

In the same way, each individual operator also pays a cost (cash outflow) when it connects to other operators' networks to reach their subscribers i.e. interconnect cost.

However, at an industry level interconnection is a zero sum game. Each operator's interconnect revenue is another operator's interconnect cost. This highlights that the industry profit pool is driven by external subscriber revenue, not by the interconnect revenue operators derive from each other.

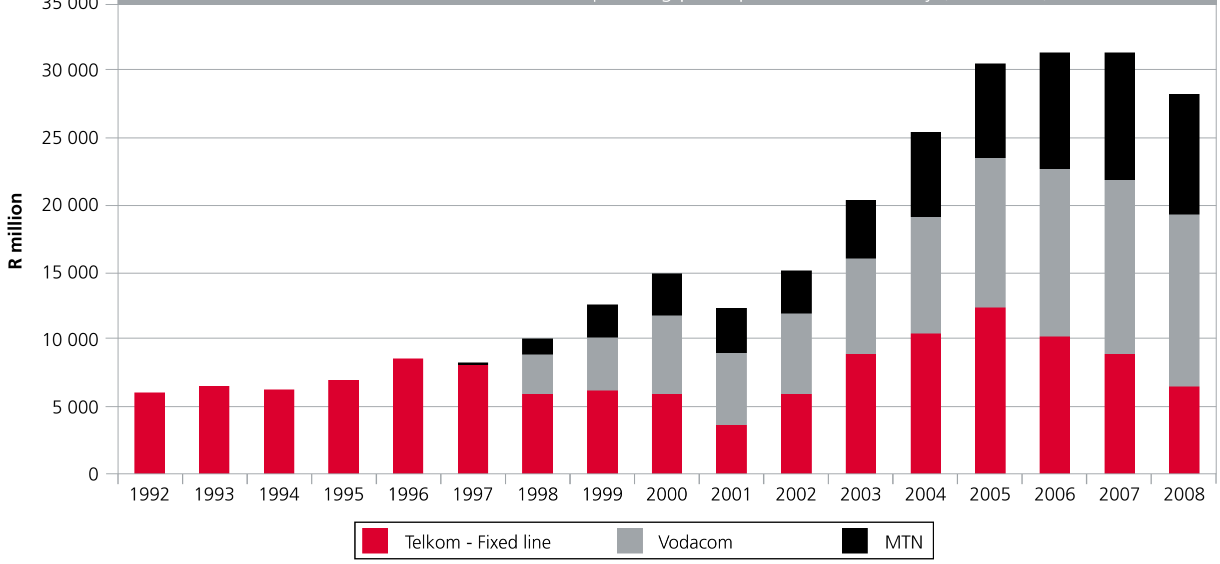
Over the past 16 years interconnect revenue (and concomitant interconnect cost) has grown faster than reported revenue. The recently announced cuts in mobile interconnection

GRAPH 2 South African telecommunications operating profit pool



Source: Company reports and Allan Gray research (Telkom/Vodacom lagged three months)

GRAPH 3 South African telecommunications operating profit pool in 2008 money (real terms)



Source: Company reports and Allan Gray research (Telkom/Vodacom lagged three months)

rates will put interconnection revenue under pressure in the future. While the reduction in mobile interconnection rates in isolation will not reduce the absolute size of the industry profit pool, it will certainly affect the distribution of those profits among market participants. Secondary effects, such as retail price pressure and increased competition, could well reduce the absolute size and distribution of industry profits.

2. Unlike revenue, the profit pool has not grown in a straight line

Despite stable revenue growth, the industry profit pool has grown significantly below trend in the past three years. The following factors have contributed to slower profit growth:

2.1 The voice market is maturing

- Voice services still contribute approximately 80% of industry revenues, but revenue growth has declined to single digits.
- The voice traffic carried on Telkom's fixed-line network has declined by approximately 25% over the past five years.
- Mobile SIM card penetration now exceeds 100% of the population, and the annual growth rate of voice traffic carried on mobile networks is declining.

2.2 Competition is increasing

- Market liberalisation: The previous regulatory framework segmented the telecommunications market by licensing narrow classes of services (voice or data) and prescribing the use of specific technologies (fixed or mobile networks) to deliver those services. The new licensing regime defines broader classes of service (voice, data and value-added services) and aims to be technology neutral. In practice, this means that the incumbent operators now compete on more levels, for example, Telkom will now offer mobile voice and data services and the mobile operators can now self-provide the fixed data links between their towers.
- Technological changes: The adoption of new technologies, such as voice over internet protocol (VoIP), has converged voice and data services. Now traditional data market participants, like the internet service provider Internet Solutions, can compete with the incumbent operators in the voice market.

3. The operating profit pool has declined in real terms

Graph 3 shows that when adjustments are made for the effects of inflation, the industry profit pool peaked in 2006 and actually declined in 2008. It is interesting to note that, in real terms, the Telkom fixed-line voice and data business currently earns a similar level of operating profit as in 1993.

In sharp contrast to the annual price increases typical of most consumer goods like food, beer, cigarettes or luxury goods, telecommunication unit prices (per minute or per megabyte) have tended to decrease over time. The main reason for this trend is that operators have shared some of the technological and scale cost benefits they have enjoyed with their customers in their efforts to attract and retain subscribers. Since 1993 the secular growth in mobile voice and data traffic volumes has more than offset the impact of declining real unit prices, resulting in increasing profits. However, in a mature and more competitive market, operators are likely to find it more difficult to manage the relationship between revenue and both operating and capital costs to their advantage. In real terms the operating profit pool may well decline further.

Investment implications

Growth in the overall telecommunications profit pool in South Africa is under pressure, and we believe that risks to forecasting future free cash flows have increased. The industry is currently attracting record levels of new capital investment. The returns generated on those investments are likely to be lower than those achieved in the past. When we evaluate listed telecommunication operators and service providers as potential investment opportunities, we consider these lower return expectations in valuing their South African operations.

A telecommunication company which has been part of our client portfolios for some time is the MTN Group. South Africa currently contributes 21% of MTN's earnings before interest, tax, depreciation and amortisation (EBITDA) and a little less than 30% of the Group's consolidated earnings. In valuing the MTN Group we consider both the headwinds faced by its subsidiary in South Africa and the remaining growth potential in relatively immature markets such as Nigeria, Ghana and Iran.

Richard Carter

Roenica Botha

UNDERSTANDING THE RETURN OF A FUND

EXECUTIVE SUMMARY: By reinvesting the income which a unit trust fund earns, investors can take advantage of the compounding effect of returns and maximise their long-term wealth creation. Richard Carter and Roenica Botha elaborate.

When we talk about a fund's performance we always assume distributions have been reinvested. But have you ever wondered how much of the performance of your fund is capital appreciation and how much is income the fund earned over the period? And what impact does reinvesting distributed income have on your long-term wealth creation?

To answer these questions it is useful to understand what a 'unit' is in a unit trust fund, and how earning and distributing income works.

What is a unit and how is it valued?

A unit represents the portion of a fund that an investor owns. Its value is calculated daily and is made up of two parts: capital and net income.

The 'capital' part is the value of the underlying shares or cash instruments the fund owns. This value is based on the price at which the underlying investments trade.

The fund earns income in the form of interest and/or dividends from its underlying investments. The fund also has expenses related to its daily management and trading. The net income (income less expenses) is accumulated daily and added to the capital value to calculate the daily unit price.

Value of the fund = Capital value of underlying investments
+ Accumulated income (interest + dividends)
- Accumulated expenses

$$\textbf{Unit price} = \frac{\text{Value of the fund}}{\text{Total number of units}}$$

> "By reinvesting the income ..., investors can take advantage of the compounding effect of returns and maximise their long-term wealth creation."

What is an income distribution and what happens when a fund distributes?

At the fund's income distribution date, all the net income which has accumulated since the previous distribution is added up and made available to be reinvested or paid out to investors as a 'declared distribution'. Since the net income forms part of the total value of the fund, when it is distributed the unit price on the day after the distribution drops by the amount distributed, plus or minus any market movement of the underlying investments for the day. If the total expenses exceed the income earned, the fund will not make a distribution, but rather has to use part of the capital in the fund to pay its expenses.

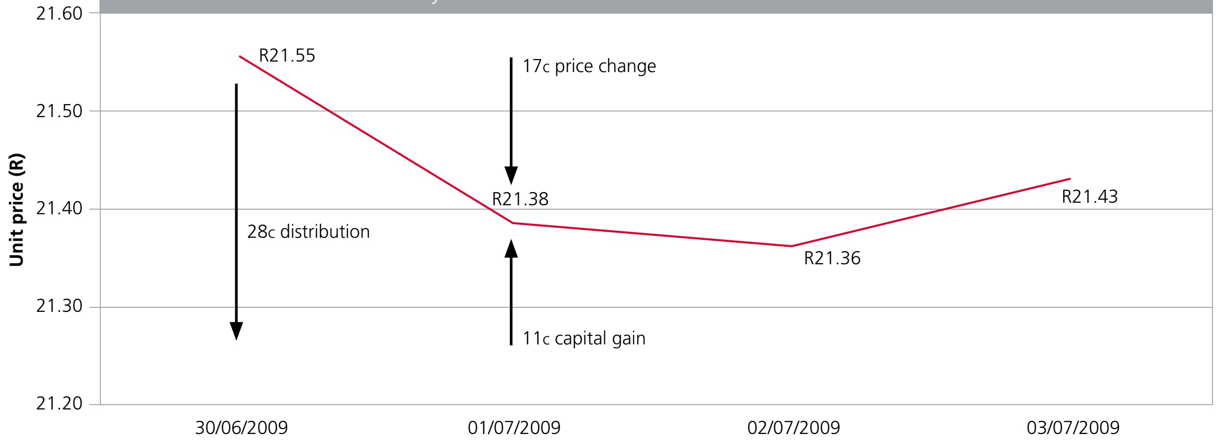
In an Allan Gray retirement product or investment platform account, distributions are automatically reinvested for investors by purchasing more units in the relevant account. This means that additional units are purchased for you with the distributed amount. The value of your holding does not change but this is made up by more units in total at a lower price per unit than before the distribution. In Allan Gray unit trust accounts, you can choose to have distributions paid out – the value of your holding in a distributing fund will reduce by the amount of any distribution paid out to you.

Example

If you look at the June 2009 distribution of the Allan Gray Stable Fund as an example:

On 30 June 2009 the Stable Fund declared a distribution of 28 cents per unit. The unit price (see **Graph 1** on page 12) on

GRAPH 1 Price of the Allan Gray Stable Fund



Source: Allan Gray research

1 July 2009 was 17 cents lower than on the previous day. This was the result of a distribution of 28 cents and an 11 cents increase in the capital value of the underlying investments.

Now consider the account of an investor who owned 1 000 Stable Fund units. On 30 June 2009, at a unit price of R21.55, the account was worth R21 553. Reinvestment of the distribution allowed the investor to buy an additional 13 units. On 3 July 2009, at a unit price of R21.43, the 1 013 units in the account was worth R21 704. This reinvestment put the investor back in the same position as on 30 June 2009 before the distribution. The additional increase was from subsequent growth in the capital value of the underlying investments.

Despite the decrease in the unit price, by reinvesting the distribution the overall value of the investment in the Stable Fund would have increased over those specific four days.

Returns from income versus capital

Table 1 shows the Allan Gray funds' returns since inception to 31 December 2008. The table breaks down the total returns into the portion earned from (a) capital and (b) the extra return you would have earned by reinvesting net distributed income (dividends + interest – expenses).

The table illustrates that the Equity Fund returns are largely of a capital nature, whereas the Money Market Fund only earns (interest) income.

The importance of reinvesting distributions

Column (b) in Table 1 shows the portion of the return earned from income and the reinvestment of that income. This can be used to see the impact on the accumulated capital value if income is paid out rather than reinvested.

R1 000 invested in the Balanced Fund since its inception (1 October 1999) would have grown to R6 570 if the investor reinvested distributions. However, if the investor had distributions paid out he would end up with R4 940, 25% less.

The impact is more marked in the Stable Fund due to the higher proportion of return earned as income. Since inception (1 July 2000) an investment of R1 000 in this Fund would have

TABLE 1 Source of return since inception

Allan Gray Fund	(a) Capital growth portion	(b) Income return (assuming reinvestment) portion
Equity	96.9%	3.1%
Balanced	83.5%	16.5%
Stable	62.0%	38.0%
Optimal	76.7%	23.3%
Money Market	0.0%	100.0%

Source: Allan Gray research

grown to R3 590 with distributions reinvested. If distributions were paid out this value would be 37% less.

In the Equity Fund, which mainly grows through capital appreciation, the difference would have been very small.

Over a longer period, the impact would be more significant because of compound interest. By reinvesting the income which a fund earns, investors can take advantage of the compounding effect of returns and maximise their long-term wealth creation.

Tax considerations

It is important to understand the nature of the returns of the funds you are invested in as there are tax implications. Income (whether it is earned from income or dividends, and whether local or foreign) is taxed differently to capital gains.

Jonathan Brodie

Trevor Black

TOUGH TO BE DIFFERENT

EXECUTIVE SUMMARY: In the Q2 Quarterly Commentary, Jonathan Brodie and Trevor Black of Orbis discussed the fact that long-term outperformance requires a partnership between the investor and the manager. Focusing on investor behaviour, they emphasised the need for investors not to chase recent winners, especially once they have carefully selected managers; instead, they should try and focus on long-term goals. This quarter they turn the spotlight on Orbis, and investment managers in general, as they take a look at the second aspect of long-term performance experience: money manager behaviour over time.

Short-term focus has become endemic. The average holding period on the New York Stock Exchange (NYSE) has dropped to just six months from three to six years in the 1970s, and closer to 10 years in the early 1940s (see **Graph 1**). Although there are many ways to make money, we think that six months is simply too short a time to capture anything much more than market noise. In our view, this is a zero-sum trading game, and quite different from our own approach to investing. While we are not 'buy and hold forever' value managers, we do give our investment theses time to play out.

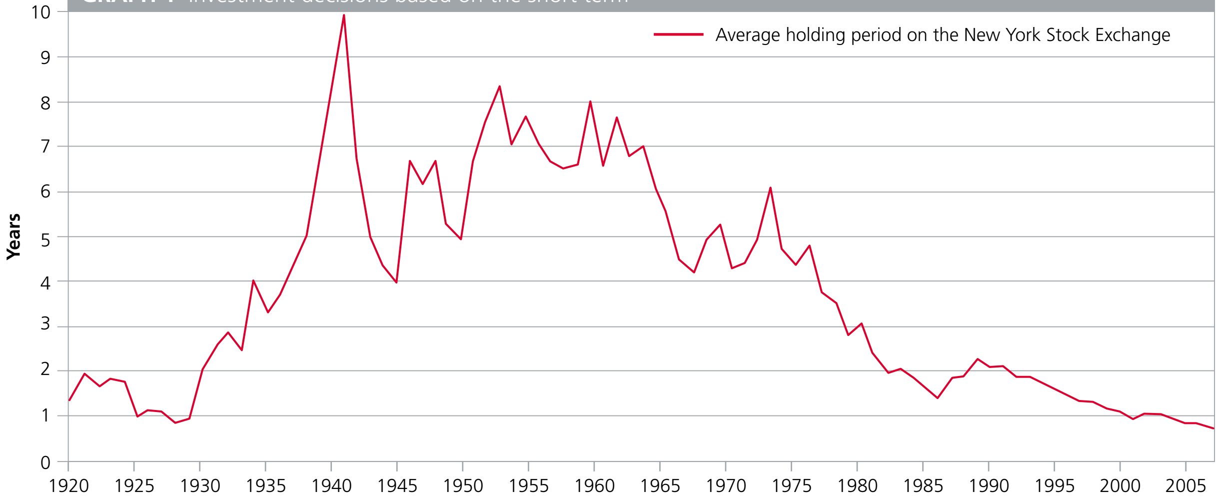
We use a 'bottom-up' approach to investing

Allan Gray and Orbis share a common investment approach and ethos. When we analyse a possible investment we look at the return we expect to receive over a four-year period. It is our experience that understanding companies and investing in them when they represent 'fundamental value' is far more rewarding than trying to predict economic, political and share market trends. Fundamental value is the value a prudent businessman would place on a business. This 'bottom-up' approach to investing involves detailed analysis of the business, its income, expenses, outlook and positioning within its industry.

The top-down model

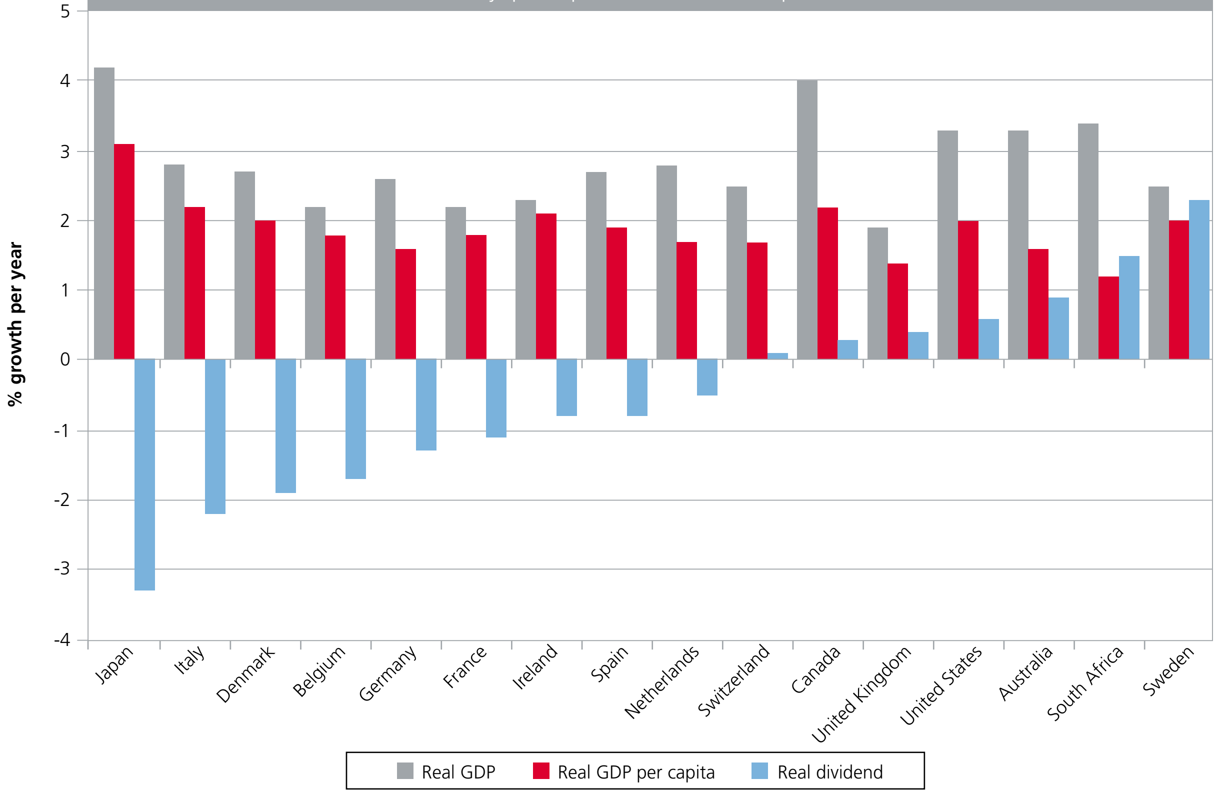
Conversely, many managers start their analysis by looking for high-growth countries or industries in the belief that these will then lead to a high-growth profit pool, which in turn will

GRAPH 1 Investment decisions based on the short term



Source: James Montier, Société Générale Global Strategy Research

GRAPH 2 Growth over the 20th century: profit pool not the same as profit share



Source: Bernstein & Arnott (2003) Financial Analysts Journal

result in attractive performance from the shares of companies with exposures to these areas. But is this top-down model a good representation of the real world over time? And how has the variation in growth rates between countries impacted on the growth in company profits in those countries? Allan Gray Chairman Simon Marais conducted some research into this question. **Graph 2** shows the overall economic growth rate and the per capita growth rate of 14 countries over the 20th century.

The analysis uses real dividend growth per share as a proxy for earnings, largely because earnings are impacted by accounting changes. Looking at the blue bars, the growth in real dividends per share over time, amazingly you see very little correlation with economic growth. If someone did you the favour of telling you which would be the winning economy over the next 100 years, it is not clear that that is of any help at all in directing your investments. Rather than overall economic conditions, or even industry trends, the profit and return performance of an individual company are importantly determined by the competitive landscape.

In a rapidly growing economy the profit cake grows quickly, but increased competition may mean your slice does not grow at all. On the other hand, a stagnating economy or industry does not attract the brightest entrepreneurs. There is little new competition and some players may well leave the industry. Often this leads to better margins for the incumbents.

How we define risk

Coupled with our contrarian approach to investing, we also have a different approach to risk. Most traditional measures look at risk as the chance of being different or more volatile than others. We define risk in terms of permanent capital loss. As a result, rather than tracking the market, what we focus on is looking obsessively at what can go wrong, looking for a 'margin of safety' and focusing on the valuation risk, earnings risk and balance sheet risk of our specific holdings. We invest in businesses when we believe their share prices are below intrinsic business value. This means we are offered some protection if things turn out worse than we forecast (i.e. a margin of safety exists). As we do not get it right all the time, by purchasing with a margin of safety we hope to minimise or avoid the loss of capital.

Because our definition of risk does not push us to look the same as the market, we are prepared to position ourselves quite differently. By way of example in terms of regions, in late 1994 Orbis was 27% overweight in the US, and in late 2003 we were 30% underweight in the US. In May 1990, we were 37% underweight in Japan, and in 1998 we were 41% overweight in Japan. The key point is that we do not look at investing from a macro perspective first. We look at companies first, and we allow our weightings to differ significantly from the market, based on our conviction in the individual selections. We are benchmark unaware.

"Although there are many ways to make money,… six months is simply too short a time to capture anything much more than market noise."

The result of this approach is that our 'tracking error', which measures how different a manager is from the crowd, can be very significant. Why would we want any 'error' in the portfolio? Despite the term, we look to maintain our tracking error over time because you cannot generate long-term outperformance successfully without being different and the tracking error is one indication of this difference. Since inception, the tracking error of the Orbis Global Equity Fund has averaged 10.1%, giving us the potential to outperform.

So what?

This all seems rather obvious. Pick stocks as you would pick a business you want to buy. Do not do what everyone else is doing. So why does everyone not do this?

The answer is at once simpler and, unfortunately, tougher than that. There is no secret formula. It takes persistence, both on the part of the analyst and the investor to sustain what many understand to be the 'right' approach. Behaving differently from the market will come to challenge your conviction. Outperformance does not come in a straight line; there are some sustained periods of disappointing performance and quite simply, we are not always correct.

The reason more people do not practise this form of investing is that they cannot withstand the pressure of being different from the crowd and of bearing the consequences of periodically being wrong. While we cannot guarantee future performance, we can come close to guaranteeing that we will again have periods where we will challenge your conviction. The only way to sustain your conviction is to understand our investment process. For our part, we continue to focus on building that process and our capacity for excellent research.

Anthony Farr

ALLAN GRAY ORBIS FOUNDATION UPDATE

EXECUTIVE SUMMARY: At the Allan Gray Orbis Foundation we have been given a rare opportunity to focus on individuals and invest in them over the long term. This long-term strategy aligns us closely with the principles prevalent at Allan Gray and Orbis. While our markets are very different, the principles surrounding the growth of capital, be it financial or human, have a lot in common. Anthony Farr elaborates, and gives an update on the Foundation's progress to date.

Over a period of 35 years, Allan Gray has consistently applied a methodology that encourages investment professionals to take a long-term approach when making their investment decisions. This approach has contributed to a track record for its equity mandate that has exceeded the market by 10% annually. A 10% increase in performance, while pleasing, may not seem significant, yet when this performance is compounded over 35 years the result is a portfolio value 21 times stronger than its benchmark (the FTSE/JSE All Share Index) achieved over the same period by the market.

If the Allan Gray Orbis Foundation facilitates a similar 10% improvement in the performance of talented individuals through our focus on education, skills, personal development, entrepreneurial thinking and the fostering of excellence and, more importantly, sustains that incremental improvement over the long term, we believe that the final outcome will be similarly exponential.

Focus on performance

A second principle we have learnt from our associated organisation is that there has always been a focus on performance, not on growing assets. Allan Gray does not set targets for assets under management, the maxim being, if one is able to achieve the performance, the assets will take care of themselves – a belief borne out by the fact that Allan Gray is now the largest private asset manager in Southern Africa.

In the context of the Foundation, 'performance' is equivalent to the quality and achievement of Allan Gray Fellows. 'Assets under management' are the number of Allan Gray Fellows in the programme. In the non-profit sector it is tempting to focus on numbers, yet, as Allan Gray has shown, a counter-intuitive focus on quality rather than quantity will ultimately end up achieving both in a more sustainable manner.

The achievements of our Fellows inspire us with hope for the future

A number of Fellows have attended youth leadership conferences in both Europe and America. Meanwhile, there were five Allan Gray Fellows out of a total of eight South African applicants up for the Dean's Award for Excellence at the UCT Commerce Faculty. This award requires academic performance at the Dean Merit List level (average in excess of 70%), in addition to all-round excellence. We are also pleased to note that a Student Health and Welfare Centre Organisation (Shawco) initiative to promote enterprise in Khayelitsha, listed six Allan Gray Fellows out of a total committee of seven, including the committee chair and deputy chair.

Graduating Allan Gray Fellows will be heading out into a variety of different careers, including honours study, accountancy articles, international banks and venture capital financial houses, while another has been accepted for the Harvard MBA (in two years time).

Finally, there has been a sense of initial completion with two of the graduated Allan Gray Fellows joining the Foundation on a six-month secondment as Fellows-in-Residence. Not too long ago they were bright-eyed students at our initial 2005 Selection Camp; a few short years later they are part of our team adding significant value before heading onto other challenges.

Twenty new graduates

The end of the 2009 academic year sees 20 Allan Gray Fellows graduating from university and our programme, joining the eight who completed last year. While each Fellow has made his/her own unique contribution, one story gives full expression to the intentions behind the Foundation:

One of seven children, this Fellow finished high school in 2005 at Sibusisiwe High School, Mpumulanga, first in her grade of 120 learners, and made her way to study engineering at Wits, the first in her family to go to university. Despite the death of both her parents during her university career, she will graduate this year as one of the very few black female civil engineers in our country, and has secured initial employment next year at one of South Africa's leading engineering firms.

> "I just had such a sudden feeling of pride and optimism about our future here!"

This Allan Gray Fellow was asked to make the year-end speech for the programme in Gauteng. In her speech she expressed much of the Foundation's aspirations:

'Our country needs leaders with character, innovation and more than anything a vision to see our fellow South Africans thrive. As Allan Gray Fellows we have been given the responsibility to be drivers of this change. As young and bright as every Fellow here is, the first step to our success is embracing this responsibility. I have been inspired by each one of you, your commitment to your dreams and ambitions, your constant hard work and the way you each see the world. More than anything I've learnt that to inspire others, you must become the change you wish to see in them. The Foundation has provided a more than filling glimpse of what hard work and commitment can achieve – we have seen the power that innovative minds wield.'

Good progress in 2009 selection campaigns

Following the early selection campaign, which resulted in 17 initial offers, (see Q2 Quarterly Commentary), the Matric campaign was completed with selection camps in late September. After these camps we offered a further 56 candidates Allan Gray Fellowships for 2010. In parallel, we completed the university selection campaign in early December. This resulted in an additional 23 Allan Gray Fellowship offers, bringing the total new Fellows for 2010 to 79.

Over the last four years we have conducted 18 selection camps at venues ranging from Robben Island to a location in the Dinokeng Game Reserve. They consistently prove to be the highlight of the Foundation's calendar. During these camps, nearly 800 of Southern Africa's most talented young leaders and innovators from four different countries have had the opportunity to test themselves at levels they might never otherwise have experienced. In treating them as future influencers, the Foundation challenges them with a regime that includes idea generation, presentations, case studies, group work, psychometric testing, constant observation, a smattering of drumming, great food and very little sleep. These ingredients create a magic mix of possibility for the candidates as they begin to realise the full potential of their generation's contribution to our region.

As one candidate commented after the camp on the Foundation's Facebook page: 'I just had such a sudden feeling of pride and optimism about our future here! If that camp is a true reflection of our generation then South Africa, have no fear! It is incredible how motivated and passionate you feel coming out of that camp!'

Meanwhile, we have started the selection campaign for the Allan Gray Scholars programme for final placement in 2011, having received over 5 000 applications by the deadline date. We will make final selection decisions in the first quarter of 2010, and those chosen will join the current 78 Scholars at the schools listed in **Table 1**.

TABLE 1 Allan Gray scholar placement schools for 2010

School	Province
Bishops Diocesan College	Western Cape
Clarendon High School for Girls	Eastern Cape
Collegiate High School for Girls	Eastern Cape
Diocesan School for Girls	Eastern Cape
Maritzburg College	Kwazulu-Natal
Paul Roos Gymnasium	Western Cape
Pietermaritzburg Girls' High School	Kwazulu-Natal
Pretoria Boys' High School	Gauteng
Rhenish Girls' High School	Western Cape
Rustenburg High School for Girls	Western Cape
Selborne College	Eastern Cape
St Alban's College	Gauteng
St Andrew's College	Eastern Cape
St Andrew's School for Girls	Gauteng
St Cyprian's School	Western Cape
St Mary's School, Waverley	Gauteng

Source: Allan Gray Orbis Foundation

There have also been pleasing developments with our sister Foundations in Namibia and Botswana. Allan Gray Orbis Foundation Namibia (nine current and awarded Allan Gray Fellows and 16 Allan Gray Scholars) and Allan Gray Orbis Foundation Botswana (six current and awarded Allan Gray Fellows) are now fully operational.

Refining our vision

We give constant thought to refining our activities and approach. One aspect that will receive renewed attention in 2010 is ensuring that Allan Gray Fellows are connected to their strengths and passions. The ultimate outcome of this work is encapsulated in the revised vision for the Foundation:

'In the coming years, there will emerge from diverse communities, a new generation of high-impact entrepreneurial leaders. Individuals of passion, integrity and innovation, who will be at the forefront of the continuing economic and social transformation of this region. These individuals will be ambassadors of the power of initiative, determination and excellence, acting as role models so that many more will follow in their pioneering footsteps.'

We know we still have a long road to travel, but the journey thus far has been full and satisfying, and we continue to seek out that additional 10% performance, remaining convinced that consistent application of the identified principles of capital creation will ultimately reap its deserved reward.

TABLE 2 Campaign dates for 2010

Allan Gray Fellowship	:	Grade 12 applications close 31 May
Allan Gray Fellowship	:	1st year university applications close 31 August
Allan Gray Scholarship	:	Grade 6 applications close 17 September (to start High School in 2012)

Source: Allan Gray Orbis Foundation

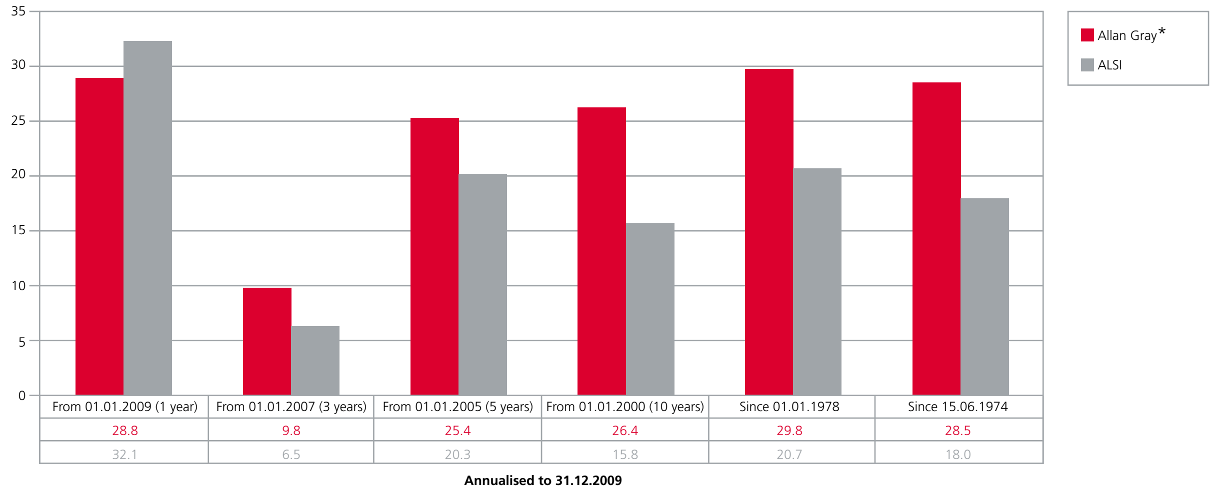
Visit our new website at www.allangrayorbis.org

One of our key marketing strategies is to develop a digital presence that will assist us in building stronger relationships with our beneficiaries and other stakeholders. We have thus relaunched our website. The new website, which provides some insights into the Foundation's opportunities, is fresh, youthful and energetic. The layout and structure make it easy to navigate. It has been built for search engine optimisation, as well as harnessing new social media for interacting with the Foundation's beneficiaries and the public.

Investment track record

Allan Gray Limited global mandate share returns vs. FTSE/JSE All Share Index

Period	Allan Gray*	FTSE/JSE All Share Index	Out/Underperformance
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 (to 31.12)	28.8	32.1	-3.3
Annualised to 31.12.2009			
From 01.01.2009 (1 year)	28.8	32.1	-3.3
From 01.01.2007 (3 years)	9.8	6.5	3.3
From 01.01.2005 (5 years)	25.4	20.3	5.1
From 01.01.2000 (10 years)	26.4	15.8	10.6
Since 01.01.1978	29.8	20.7	9.1
Since 15.06.1974	28.5	18.0	10.5
Average outperformance			10.5
Number of calendar years outperformed			27
Number of calendar years underperformed			8



* 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.

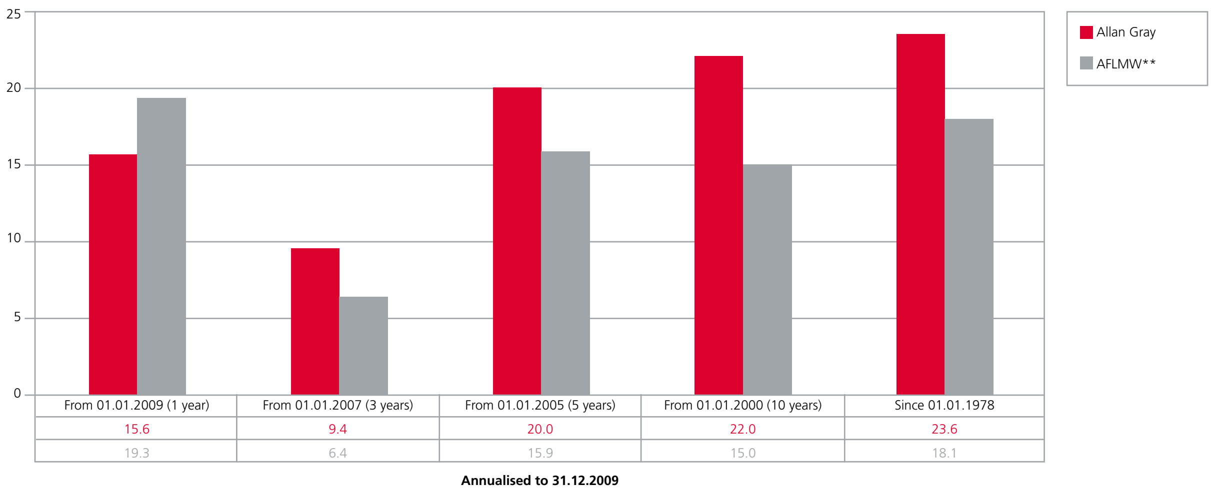
Note: Listed property included from 1 July 2002.

An investment of R10 000 made with Allan Gray on 15 June 1974 would have grown to **R73 583 612** by 31 December 2009. By comparison, the returns generated by the FTSE/JSE All Share Index over the same period would have grown a similar investment to **R3 570 454**.

Investment track record

Allan Gray Limited global mandate total returns vs. Alexander Forbes Large Manager Watch

Period	Allan Gray	AFLMW**	Out/Underperformance
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 (to 31.12)	15.6	19.3	-3.7
Annualised to 31.12.2009			
From 01.01.2009 (1 year)	15.6	19.3	-3.7
From 01.01.2007 (3 years)	9.4	6.4	3.0
From 01.01.2005 (5 years)	20.0	15.9	4.1
From 01.01.2000 (10 years)	22.0	15.0	7.0
Since 01.01.1978	23.6	18.1	5.5
Average outperformance			5.5
Number of calendar years outperformed			25
Number of calendar years underperformed			7



** Consulting Actuaries Survey returns used up to December 1997. The return for December 2009 is an estimate.

An investment of R10 000 made with Allan Gray on 1 January 1978 would have grown to **R8 768 276** by 31 December 2009. The average total performance of global mandates of large managers over the same period would have grown a similar investment to **R2 030 621**.

Allan Gray annualised performance in percentage per annum to 31 December 2009	FOURTH QUARTER (unannualised)
UNIT TRUSTS[1]	
EQUITY FUND (AGEF)	[3]
FTSE/JSE All Share Index	
BALANCED FUND (AGBF)	[3]
Average of both Prudential Medium Equity category and Prudential Variable Equity category (excl. AGBF)	
STABLE FUND (AGSF) - (NET OF TAX)	[3]
Call deposits plus two percentage points (Net of tax)	
STABLE FUND (AGSF) - (GROSS OF TAX)	[3]
Call deposits plus two percentage points (Gross of tax)	
MONEY MARKET FUND (AGMF)	[3]
Domestic fixed interest money market unit trust sector (excl. AGMF)	
OPTIMAL FUND (AGOF)	[3]
Daily call rate of FirstRand Bank Ltd	
BOND FUND (AGBD)	[3]
BEASSA All Bond Index (total return)	
GLOBAL FUND OF FUNDS (AGGF)	[3]
60% of the FTSE World Index and 40% of the JP Morgan Global Government Bond Index (Rands)	
GLOBAL EQUITY FEEDER FUND (AGOE)	[3]
FTSE World Index (Rands)	
LIFE POOLED PORTFOLIOS	
GLOBAL BALANCED PORTFOLIO	**5.0**
Mean of Alexander Forbes Global Large Manager Watch [2]	4.8
DOMESTIC BALANCED PORTFOLIO	**6.6**
Mean of Alexander Forbes Domestic Manager Watch [2]	6.1
DOMESTIC EQUITY PORTFOLIO	**9.0**
FTSE/JSE All Share Index	11.4
DOMESTIC ABSOLUTE PORTFOLIO	**4.2**
Mean of Alexander Forbes Domestic Manager Watch [2]	6.1
DOMESTIC STABLE PORTFOLIO	**3.1**
Alexander Forbes Three-Month Deposit Index plus 2%	2.2
DOMESTIC OPTIMAL PORTFOLIO [1]	**2.5**
Daily Call Rate of Nedcor Bank Limited	1.6
GLOBAL ABSOLUTE PORTFOLIO	**2.6**
Mean of Alexander Forbes Global Large Manager Watch [2]	4.8
DOMESTIC MEDICAL SCHEME PORTFOLIO	**2.9**
Consumer Price Index plus 3% p.a. [2]	0.8
GLOBAL STABLE PORTFOLIO	**1.1**
Alexander Forbes Three-Month Deposit Index plus 2%	2.2
RELATIVE DOMESTIC EQUITY PORTFOLIO	**11.6**
FTSE/JSE CAPI Index	11.3
MONEY MARKET PORTFOLIO [1]	**2.0**
Alexander Forbes Three-Month Deposit Index	1.7
FOREIGN PORTFOLIO [1]	**-4.6**
60% of the MSCI Index and 40% JP Morgan Global Government Bond Index (Rands)	-0.2
ORBIS GLOBAL EQUITY PORTFOLIO [1]	**-0.1**
FTSE World Index (Rands)	2.1
SEGREGATED PORTFOLIOS [5]	
GLOBAL BALANCED COMPOSITE	**4.8**
Mean of Alexander Forbes Global Large Manager Watch [2, 4]	4.8
DOMESTIC BALANCED COMPOSITE	**6.6**
Mean of Alexander Forbes Domestic Manager Watch [2]	6.1
DOMESTIC EQUITY COMPOSITE	**8.7**
FTSE/JSE All Share Index	11.4
GLOBAL BALANCED NAMIBIAN HIGH FOREIGN COMPOSITE	**2.5**
Mean of Alexander Forbes Namibia Average Manager [2]	4.8
RELATIVE DOMESTIC COMPOSITE	**10.7**
Weighted average of client specific benchmarks [2]	10.7
FOREIGN BEST VIEW (RANDS) COMPOSITE	**-3.1**
60% of the MSCI and 40% of the JP Morgan Global Government Bond Index (Rands)	-0.2
ORBIS FUNDS (RANDS) [1, 6]	
ORBIS GLOBAL EQUITY FUND (RANDS)	**-0.1**
FTSE World Index (Rands)	2.1
ORBIS JAPAN EQUITY (YEN) FUND (RANDS)	**-11.2**
Tokyo Stock Price Index (Rands)	-5.4
ORBIS OPTIMAL SA FUND-US$ CLASS (RANDS)	**-3.0**
US$ Bank Deposits (Rands)	-2.2
ORBIS OPTIMAL SA FUND-EURO CLASS (RANDS)	**-4.1**
Euro Bank Deposits (Rands)	-3.5
ORBIS ASIA EX-JAPAN EQUITY FUND (RANDS)	**3.6**
MSCI Asia Ex-Japan (Rands)	4.2

PERFORMANCE AS CALCULATED BY ALLAN GRAY

1 The fund returns are net of investment management fees
2 The return for Quarter 4, 2009 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
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

1 YEAR	3 YEARS	5 YEARS	10 YEARS	SINCE INCEPTION	ASSETS UNDER MANAGEMENT (R million)	INCEPTION DATE
21.6	6.1	20.8	22.1	30.8	21 437.5	01.10.98
32.1	6.5	20.3	15.8	19.7		
14.0	8.2	17.6	20.0	21.7	32 387.7	01.10.99
16.5	5.8	14.0	13.0	14.5		
5.6	8.9	12.4	-	13.9	30 514.7	01.07.00
7.3	8.3	7.4	-	7.9		
6.8	10.0	13.4	-	15.2	30 514.7	01.07.00
9.8	11.2	9.9	-	10.6		
9.2	10.3	9.1	-	9.5	8 544.6	03.07.01
9.1	10.1	8.9	-	9.5		
6.5	9.4	9.1	-	9.7	2 771.5	01.10.02
7.6	9.0	7.7	-	8.1		
5.7	8.0	7.9	-	8.9	161.8	01.10.04
-1.0	6.5	7.2	-	8.3		
-3.9	7.5	13.2	-	8.4	6 708.6	03.02.04
-4.8	3.2	10.3	-	6.6		
11.8	2.6	-	-	12.0	3 708.7	01.04.05
5.8	-2.2	-	-	7.8		
16.0	9.5	20.0	-	22.2	14 546.5	01.09.00
19.3	6.4	15.9	-	15.4		
20.5	10.3	21.8	-	22.9	5 604.8	01.09.01
23.6	8.2	17.3	-	18.0		
25.7	9.5	25.1	-	26.7	6 034.4	01.02.01
32.1	6.5	20.3	-	16.8		
19.5	15.3	24.0	-	26.7	546.6	06.07.01
23.6	8.2	17.3	-	17.5		
13.5	12.4	16.5	-	17.4	1 125.1	01.12.01
10.8	12.1	11.0	-	11.7		
7.7	10.6	10.2	-	10.0	836.7	04.12.02
7.9	9.4	8.1	-	8.2		
13.6	14.6	23.2	-	22.3	1 389.6	01.03.04
19.3	6.4	15.9	-	17.8		
13.0	12.1	15.2	-	16.1	1 075.2	01.05.04
9.2	11.4	10.0	-	9.4		
7.5	11.1	15.2	-	16.3	2 835.0	15.07.04
10.8	12.1	11.0	-	10.9		
30.1	9.2	23.4	-	27.6	406.5	05.05.03
32.3	7.2	20.7	-	25.4		
9.5	10.4	9.2	-	9.9	741.1	21.09.00
8.6	9.9	8.8	-	9.6		
-5.1	7.0	13.3	-	5.0	1 408.1	23.01.02
-4.4	3.2	10.3	-	1.2		
11.5	2.9	14.0	-	12.0	2 268.4	18.05.04
5.8	-2.2	9.4	-	8.2		
15.6	9.4	20.0	22.0	23.6	25 259.3	01.01.78
19.3	6.4	15.9	15.0	18.1		
20.5	10.3	21.7	22.8	24.1	21 158.6	01.01.78
23.6	8.2	17.3	16.5	18.6		
25.8	9.9	25.3	25.6	22.8	45 981.2	01.01.90
32.1	6.5	20.3	15.8	15.1		
10.6	10.4	19.4	21.6	20.8	5 427.1	01.01.94
18.9	8.3	16.5	15.1	14.8		
29.0	8.1	22.2	-	23.2	10 739.4	19.04.00
31.5	6.3	19.5	-	16.9		
-3.2	5.9	12.6	17.3	14.9	5 222.0	23.05.96
-4.4	3.2	10.3	5.5	10.4		
11.4	2.6	14.2	13.0	19.2	-	01.01.90
5.8	-2.2	9.4	2.9	12.0		
-15.6	-2.0	6.8	5.8	13.5	-	01.01.98
-17.3	-8.2	4.4	-2.7	5.5		
-11.9	8.1	-	-	12.0	-	01.01.05
-21.0	5.0	-	-	9.2		
-10.4	10.7	-	-	12.4	-	01.01.05
-18.7	8.3	-	-	9.8		
54.6	13.2	-	-	19.4	-	01.01.06
35.4	6.7	-	-	15.4		

Allan Gray Balanced Fund Quarterly Disclosure as at 31 December 2009

	% of Fund
South African equities	**49.2**
Resources	**12.2**
Sasol	4.3
Anglogold Ashanti	4.0
Harmony Gold Mining Co.	1.6
African Rainbow Minerals	1.4
Positions individually less than 1% of total JSE-listed securities held by the Fund	0.8
Financials	**7.6**
Sanlam	3.0
Standard Bank Group	1.5
Reinet Investments SA	0.9
Firstrand	0.7
Positions individually less than 1% of total JSE-listed securities held by the Fund	1.5
Industrials	**29.1**
SABMiller	7.3
Remgro	3.5
MTN Group	2.3
Sappi	2.1
Compagnie Fin Richemont SA	1.9
Dimension Data Holdings	1.4
Nampak	1.3
Illovo Sugar	1.2
Sun International	1.0
Tongaat-Hulett	0.9
Shoprite Holdings	0.7
Mondi Limited	0.6
Netcare	0.6
Positions individually less than 1% of total JSE-listed securities held by the Fund	4.2
Other securities	**0.3**
Positions individually less than 1% of total JSE-listed securities held by the Fund	0.3
Derivatives	**-1.3**
ALSI 40 0310-RMB	-1.3
---- Net South African equities ----	*47.9*
Hedged South African equities	**1.3**
Commodities	**3.9**
New Gold ETF	3.9
Bonds	**4.8**
RSA Bonds	1.9
Parastatal Bonds	0.2
Corporate Bonds	2.8
Money market and call deposits	**22.6**
Foreign - JSE inward listed shares	**3.9**
British American Tobacco	3.9
Foreign - Orbis absolute return funds	**7.8**
Orbis Optimal SA Fund (US$)	4.9
Orbis Optimal SA Fund (Euro)	2.9
Foreign - Orbis equity funds	**7.8**
Orbis Global Equity Fund	4.8
Orbis Japan Equity Fund (Yen)	3.0
Totals:	**100.0**

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

Total Expense Ratios (TERs)

	Equity Fund	Balanced Fund	Stable Fund	Optimal Fund	Bond Fund	Money Market Fund	Global Fund of Funds	Global Equity Feeder Fund
Performance component	1.30%	0.59%	0.14%	0.34%	0.14%	0.00%	0.72%	0.68%
Fee at benchmark	1.71%	1.15%	1.14%	1.14%	0.29%	0.29%	1.28%	1.49%
Trading costs	0.13%	0.08%	0.07%	0.36%	0.00%	0.00%	0.17%	0.18%
Other expenses	0.01%	0.01%	0.01%	0.01%	0.08%	0.01%	0.06%	0.05%
Total Expense Ratio (TER)	3.15%	1.83%	1.36%	1.85%	0.51%	0.30%	2.23%	2.40%

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 the end of September 2009. 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.