FOREWORD

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DID YOU KNOW? ALGO TRADING

"Algo trading," derived from the term "algorithmic trading," involves computers programmed to trade securities on criteria such as price movements or the volume of securities being traded. It has been estimated that as much as one third of all EU and US stock trades are driven by algorithmic programmes.

A special case of algo trading is "high frequency trading" whereby computers are programmed to initiate trades based on receipt of electronic information. They are able to transact before human market participants can even begin to process the new information.

Proponents argue that algo trading is good for markets in that it promotes market liquidity. Long-term investors generally oppose algo trading, since it doesn't assist with price discovery and can dangerously perpetuate a contagion effect. Because transactions are not initiated from fundamental value decisions, algo trading is contrary to the true nature of investing.

EQUITIES - A CLASS ACT

The Foord Balanced and Foord Flexible Funds have significant weightings to shares because they are the most attractive asset class on a three to five year view. Yet investors' confidence in share investments is often tested when markets are volatile or weak. The past quarter is a typical example. MIKE SOEKOE advises investors to ignore short-term volatility and focus on the long-term growth prospects of share investments.

Cash plays an important role in a portfolio: it serves as a shock absorber during times of volatility, while providing liquidity for client-requested withdrawals and purchases of investments as they become cheaper. But cash is not an attractive long-term investment because over time it only marginally outperforms inflation.

To achieve inflation-beating capital growth, investors must invest in securities with growing distributions such as shares. However, most investors only feel vindicated in this decision when share prices are rising quickly. Unfortunately, the convergence of a share's price and its true value may take much longer than anticipated. This often leads to disappointment and premature withdrawals from savings portfolios into the trusted "safe haven" of cash.

South Africa (and the world in general) is currently experiencing low interest rates. In such an environment, growing dividends from shares are important in the investment process. The short-term benefit is that dividend yields on many listed companies are similar to the after-tax yields from cash. But the longer-term benefits from investing in shares are where the greatest opportunities lie.

Consider the following scenario and set of assumptions. A portfolio of quality JSE listed shares currently has a dividend yield of 3.5%. Realistically, the earnings of these companies (and therefore their dividends) should grow by at least 12.5% per annum over the next seven years. Assume that share prices remain stable and assume an average cash yield of 7.5% over the next seven years.

For every R1,000 currently invested, a dividend of R35 was received over the last year. However, this more than doubles to R80 per year after seven years, given the annual growth in dividends of 12.5%. This equates to an 8% yield on original capital, which exceeds the prevailing cash yield of 7.5%.

> "TO ACHIEVE INFLATION-BEATING CAPITAL GROWTH, INVESTORS MUST INVEST IN SECURITIES WITH GROWING DISTRIBUTIONS SUCH AS SHARES."

This simple example proves an important point: investing into assets which have growing distributions, such as shares, allows an investor to remain invested in her pre-retirement savings portfolio once she decides to retire. She needn't worry about volatility or switching to cash. The benefits of shares in a wealth creation strategy become even more appealing assuming some capital appreciation (increases in share prices).

So when should investors reduce their equity holdings? We recommend that only in periods of extreme overvaluation should a significant reduction in equity exposure be considered, in particular when future returns are severely compromised. This is not the case currently. Investors saving for the long term should continue to hold a fair weight in quality companies. This can be achieved through an investment into the Foord Flexible or Foord Balanced Funds.

WEALTH PRESERVATION - BEATING THE EVILS OF INFLATION

The consensus in the market is that inflation has troughed. Expectations are that higher commodity prices and surges in certain administered costs and taxes will cause the domestic inflation rate to rise - with an increase from the current 4.6% towards the 6% upper end of the inflation target, or higher. And as WILLIAM FRASER points out, inflation means that incomes have to grow much faster than outlays in order to maintain a constant standard of living.

The preservation of capital in real terms must form the core of investment philosophies if one wants to beat the evils of inflation. Investors must select investments that have the ability to grow their values over time. Such growth comes through increases in the price of the investment (capital growth) and through increases in annual income payments (dividends or interest). This is particularly true in the present environment, where nominal interest rates are very low, both domestically as well as globally. Interest rates are also falling in real terms because rising inflation is not immediately offset by rising interest rates.

Interest yields are generally insufficient to cover the risk that inflation will be higher than the market expects. Therefore, one must seek alternatives to investments in the cash and traditional bond markets.

Our advice to investors is to search for assets on high yields, where the payments are highly predictable, capital is safe and importantly, incomes can grow over time. Investments that meet these requirements are often not in traditional interest bearing instruments like the cash and bond markets. They are therefore often overlooked as options to grow income and capital.

> “RISING INFLATION IS NOT IMMEDIATELY OFFSET BY RISING INTEREST RATES.”

INFLATION BEATING OPTIONS

Listed property instruments have typically delivered returns well above inflation. In the early part of the millennium, yields were attractive and price appreciation has accounted for a large portion of the total real returns achieved over the last decade. Despite much lower yields compared to 10 years ago, the fundamental approach to listed property as an asset class hasn't changed. The addition to portfolios of good quality listed property companies with attractive yields increases the probability of producing inflation-beating returns. Annual escalations in rentals of around 8 to 9% per annum are still the norm in this sector and over time, this growth in rental income should provide for growth in distributions to investors that are above inflation.

In the current low interest rate environment, cash flush companies are able to return a significant amount of earnings to shareholders. Looking forward 12 to 18 months, dividend yields should approach cash rates in many cases. Importantly, dividends are real, while cash yields are nominal. Investing in companies that can pass on rising input costs to their customers is important - especially in a rising inflation environment. Equally important is to trust the management teams of companies to deal with issues like rising prices.

Investors should generally seek to support management teams which have dealt successfully with previous episodes of rising inflation. Dividends are an important component of total investment returns. Investing in companies where dividends grow over time provides additional certainty in maintaining one's standard of living.

Growing income from investments is an important component in the wealth creation process. It provides a more certain investment outcome than bonds or cash, where one assumes significant inflation risk. Listed property with growing distributions and shares with growing dividends are critical to the success of achieving returns which beat inflation. This is particularly true in times when the outlook for inflation is negative and mispriced.

SKILLS SHORTAGE ADDRESSED AT GRASS ROOTS

The continuing skills shortages experienced in SA, particularly in the financial and wealth management sectors, has seen many organisations battling to recruit suitable employees with the right qualifications and skills. Foord is supporting a variety of educational initiatives that invest in the skills of the next generation. MIKE SOEKOE studies these initiatives a little closer.

Founded in 2003, LEAP is the only privately funded maths, science and technology school in South Africa. It aims to transform disadvantaged communities throughout SA via education initiatives focused on mathematics and science. The school partners with specific communities to provide their children with the opportunity to gain access to tertiary study opportunities.

> "IT IS ESSENTIAL TO SUPPORT EDUCATIONAL INITIATIVES IF WE ARE TO ADDRESS THE ISSUES OF SKILLS SHORTAGES AND UNEMPLOYMENT IN SA."

The school currently relies on private funding and donors and Foord identified the school's need to establish an endowment fund to provide ongoing financial support in the long term. Foord contributed seed capital to an endowment fund which Foord manages free of charge. It is hoped that over time, through contributions and superior investment returns, the endowment fund will grow to be substantial, resulting in a sustainable income source for the school.

Foord also sponsors a chair in investments at Rhodes University. This chair aims to promote the study and understanding of investments and investment management. Foord hopes that the subject of investments will be included in as many degree courses as possible. This will ensure broad-based understanding of the subject, which we believe to be a critical skill.

Our sponsorship of an investments chair is a specific strategy. Rather than endorse bursaries from which just a handful of students may benefit, we believe that funding one skilled and passionate educator will provide life-skill learning to a far greater number of people.

Foord is also committed to the support of a non-profit organisation called Bridge, which aims to build the capacity of the education system to expand, to adopt working practices and emerge into a resilient performing platform. The organisation concentrates on the four areas of school leadership and management; teacher development, accountability and evaluation; addressing socio-economic barriers to learning and the provision of teaching materials and early childhood development. In May 2010, Foord committed to funding the cost of employing a Chief Executive Officer for a three-year period and in June of the same year, Bridge appointed Ms Linda Vilakazi-Tselane to the position of CEO.

At Foord we believe that it is essential to support educational initiatives if we are to address the issues of skills shortages and unemployment in SA.

MAKING THE BENCHMARK AT FOORD

MARK HODGES

This quarter we bid a sad farewell to an important member of the Foord team. MARK HODGES made the tough decision to retire earlier this year. Paul Cluer pays tribute to this bastion of the firm.

Mark joined Foord way back in November of 1987. Over the course of the last 23 years, he has worked tirelessly in the best interests of the staff, shareholders and most notably all our many and varied clients. He has been a pillar of the firm for each of those 23 years and it is fair to say that Foord would not be the company it is today without Mark.

It is difficult for me to express in words Mark's enormous contribution to Foord over the years. The easy part is to note his involvement in the accounting, finance, HR and portfolio administration areas; the value he has added as a research analyst, portfolio manager and mentor; his careful handling of clients and acute focus on client service; his strategic impact as a director of Foord Asset Management, Foord Unit Trusts and Foord Compass; the care with which he has overseen the staff's own retirement fund investments as Chairman of the Foord Umbrella Provident Fund; and his involvement in projects too numerous to list including Foord's Namibia venture and Foord's two BEE joint venture initiatives.

In my view, the more challenging part is to convey the impact of Mark's strong code of ethics, principles and integrity; of always doing the right thing no matter the consequence; of his fair dealing of all parties in any dispute; of the extent of his care for clients and staff; and of his unwavering dedication to the well-being of Foord Asset Management.

While companies, staff, systems and processes all change and evolve, Mark's lasting legacy in my view will be his contribution to the Foord culture which encompasses all of these principles – in large part due to Mark's steady influence over the years.

While Mark will relinquish his executive duties at Foord Asset Management and his directorship of Foord Compass, it is pleasing that he will maintain regular contact through his continued involvement on the board of Foord Unit Trusts in a non-executive capacity.

In celebration of his career at Foord, Mark and his wife, Liz, will be enjoying a three week dream safari through south-eastern and east Africa in August. The safari culminates in a tented camp located on the northern border of the Masai Mara game reserve – with an opportunity to witness Africa's great migration.

Mark, from the directors and staff at Foord, thank you for a job superbly done. We all wish you a fantastic holiday, and everything of the best and more as you pursue your many other passions and interests in life.

IN A NUTSHELL

BRUCE ACKERMAN and WILLIAM FRASER wrap up the markets for the second quarter of the year.

INTERNATIONAL

EQUITIES

Developed market equities recovered sharply in April (Europe and Japan more so than USA) after the March Japanese quake selloff – but fell in May and June on evidence of weaker economic activity and as Greek debt default fears intensified

BONDS

Bond yields fell as lower commodity prices alleviated inflation fears – and because of increased demand for safe haven assets as Greek sovereign debt default concerns rose

CURRENCIES

The euro initially rose strongly on higher Eurozone interest rates but weakened latterly on US dollar demand as concerns about Greece intensified – but recovered at quarter-end as Greece cleared legislative hurdles to avoid immediate bankruptcy

COMMODITIES

Commodity prices abated on slower growth concerns and as speculative positions unwound, although gold rose – while oil prices fell sharply as the IEA released stockpiles to (temporarily) offset Libyan supply loss

ECONOMY

In the Eurozone, only Germany and France experienced strong growth – while the US recovery faces employment headwinds and Japan remains mired in recession

MONETARY AND FISCAL POLICY

In the USA, Bernanke has heralded no further stimulus measures to support the already below-par recovery, although low interest rates persist – while in Europe accommodative rates continue despite the ECB increasing interest rates by 0.25% to 1.25%

SOUTH AFRICA

EQUITIES

The JSE tracked global emerging markets lower on increased risk aversion following growing Greek default concerns – but resource counters fell sharply on lower commodity prices

BONDS

Bond yields fell – as risk aversion globally resulted in lower yields, while foreign demand for SA bonds remains high

CURRENCIES

The rand remained strong notwithstanding commodity price declines – because of the strong gold price and continued net foreign inflows into the high-yielding domestic bond market

ECONOMY

Economic activity surprised positively – as a broader based consumer recovery takes hold and on early signs that fixed capital formation has possibly turned the corner

MONETARY AND FISCAL POLICY

Interest rates were unchanged – despite rising inflation and high commodity prices, as economic activity continues to be below potential

FOORD FLEXIBLE FUND OF FUNDS

INVESTMENT RETURNS

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	6.7	8.9	15.5	1.0
Benchmark	12.0	11.2	9.5	3.3

Benchmark: CPI + 5% per annum, which is applied daily by using the most recently available inflation data and accordingly will be lagged on average by 5 to 6 weeks.
Inception date: 1 April 2008

OBJECTIVE

To provide investors with real returns exceeding 5% per annum, measured over rolling three-year periods. The fund will exploit the benefits of global diversification in a portfolio that continually reflects Foord Asset Management's prevailing view on all available asset classes, both in South Africa and abroad. The fund is suitable for investors with a moderate risk profile who require long-term inflation beating total returns, but who do not require a high income yield.

FOORD INTERNATIONAL FEEDER FUND

INVESTMENT RETURNS

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	6.7	-2.8	3.0	0.2
Benchmark	4.9	-3.7	16.3	0.5

Benchmark: The ZAR equivalent of the MSCI World Equities Index (developed markets)
Inception date: 1 March 2006

OBJECTIVE

To provide exposure to a portfolio of international securities constructed with the purpose of maximising return with minimum risk. This is achieved through direct investment into the Foord International Trust, which aims to produce an annualised return over time in excess of 10% in US dollars, thereby expecting to outperform world equity indices. The fund is suitable for South African investors who seek to diversify their portfolios offshore and to hedge against rand depreciation.

FOORD BALANCED FUND

INVESTMENT RETURNS

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	17.0	8.5	15.8	0.8
Benchmark	14.9	8.2	11.6	0.4

Benchmark: The market value weighted average total return of the Domestic Asset Allocation Prudential Variable Equity unit trust sector, excluding Foord Balanced Fund.
Inception date: 1 September 2002

OBJECTIVE

The steady growth of income and capital, as well as the preservation of real capital (being capital adjusted for the effects of inflation). The fund is managed to comply with the prudential investment limits set for retirement funds in South Africa (Regulation 28 to the Pension Funds Act). The fund is suitable for pension funds, pension fund members, holders of contractual savings products, medium- to long-term investors and those investors who require the asset allocation decision to be made for them, within prudential investment guidelines.

FOORD EQUITY FUND

INVESTMENT RETURNS

	Since Inception %	3 Years %	1 Year %	3 Months %
Foord*	20.5	11.2	25.4	1.1
Benchmark	17.8	4.5	24.6	-0.6

Benchmark: Total return of the FTSE/JSE All Share Index
Inception date: 1 September 2002

OBJECTIVE

To earn a higher total rate of return than that of the South African equity market, as represented by the return of the FTSE/JSE All Share Index including income, without assuming greater risk. The fund is suitable for investors who require maximum long-term capital growth and who are able to withstand investment volatility in the short to medium-term.

NOTE: Investment returns for periods greater than 1 year are annualised   * Net of fees and expenses

PLEASE REFER TO THE FACT SHEETS CARRIED ON WWW.FOORD.CO.ZA FOR MORE DETAILED INFORMATION.