FOREWORD

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DID YOU KNOW? LIQUIDITY

Liquidity refers to the ease by which an investment can be converted into cash. The concept embraces both speed and price. In deep, liquid markets, assets can be sold very quickly with very little price impact.

In South Africa, the JSE Limited is regarded as a liquid market, with many buyers and sellers transacting huge sums daily. That said, not every stock is liquid. Some small and microcap stocks have very little free float and do not often trade. Small trade volumes can produce large price swings.

The JSE's debt markets are very liquid and well developed in terms of number of participants and daily trade. South African government bonds account for most of the average R15 billion of debt instruments traded daily. It is quite easy to sell a well-traded bond instrument quickly into the market in large quantities with very little, if any, price impact.

IN THIS ISSUE

IT'S TIME IN THE MARKET THAT COUNTS

DAVE FOORD Chief Investment Officer

"After a period of underperformance in 2017 and 2018, I feel compelled to thank investors for their patience and placing their trust in Foord. We take the stewardship of investments very seriously and look after investors' savings with the same level of duty and care as we do our own.

Foord's recent SA equity performance was terrible compared to our history and high standards. It is only the second time it has happened to us in 40 years. We are not comfortable with that; we are very unhappy about it. Part of the underperformance was timing, which is already unwinding. Headwinds in some instances are becoming tailwinds.

As Chief Investment Officer of Foord's South African and global operations, I am intimately involved with the investment decisions on all portfolios. There are seven multiple-counsellor portfolio managers at Foord besides me. Each has from four to 15 years' experience at Foord. Aggregate investment experience approaches 200 years. We have a team of seasoned analysts supporting them.

Foord is an investment house, not merely an equity house. Our asset allocation calls have been very good and are increasingly vindicated. The asset allocation funds we manage across the full equity spectrum (Foord Flexible, Foord Balanced, Foord Conservative and Nedgroup Investments Stable Funds) have performed very well this year and over all long-term periods that matter, despite poor short-term SA equity selection.

Foord Flexible is top ranked in its sector since its April 2008 launch. Foord Balanced is in the top five funds over 15 years, Foord Conservative is top quartile over its five-year life and Nedgroup Investments Stable Fund which Foord has managed from its inception is first over ten years.

We are not complacent; my team and I are committed to doing the best we can for our investors. We continue to improve our investment processes as we seek to manage investment risks before chasing returns.

The portfolios are all cautiously constructed within their respective mandates as we emphasise capital preservation at this point in the cycle. Over 20% of the average long-term equity and 80% of the average long-term listed property allocation is on standby awaiting a buying opportunity (for now invested in medium-dated bonds earning inflation plus 5%). Cash, bonds and dollar cash proxy assets make up around 40% of the multi-asset portfolios.

Depending on the fund, from 45% to 75% of the portfolio is invested in the Foord global funds and rand hedge counters, which protect investors against currency depreciation and consequent inflationary pressures.

We prefer the earnings prospects and resilience of global equities and JSE-listed overseas companies to SA companies exposed to the weak local economy. We nevertheless hold some protection against a large decline in the US S&P 500 index.

The funds are exceptionally well diversified and positioned for risks and opportunities that lie ahead. Please be patient, stay invested and apply "wait" to the asset class weighting. We expect to achieve outsized returns again in the years ahead. Thank you for your continued support."

PRESERVING INVESTOR CAPITAL – THE FOORD WAY

WILLIAM FRASER Portfolio Manager

Capital preservation is fundamental to compounding long-term inflation-beating returns. WILLIAM FRASER explains the importance of liquidity (see *Did You Know?*), patience, objective thinking and flexibility.

Capital preservation strategies differ from person to person. The most risk-averse investors may hoard their cash under the proverbial mattress. But bank or money market fund deposits that earn interest periodically with capital returned at maturity are most common.

Astute investors will however recognise the long-term limitations of these cash-based strategies:

- Short-term interest rate instruments offer a low real return before tax and often a negative return after tax and inflation
- They are not "risk free" as bank failures do happen, resulting in partial or total impairment of the investor's deposit (banks with riskier business models lure depositors by offering higher-than-market interest rates)
- Longer duration (length of time) deposits that allow for higher interest rates also increase the probability of variances in the market value of the capital invested, often more than expected by risk-averse investors.

Cash and short-duration interest instruments thus rarely outperform growth assets such as shares or listed property over longer term periods.

Cumulatively, when measuring all rolling five-year returns since 1960, bonds and cash have outperformed growth assets less than 20% of the time. But these periods are infrequent and short-lived (see graph).

Investors are now experiencing a rare period where cash and bonds are outperforming growth assets over the past 12 months and even five years (measured to the end of September 2019). It is therefore unsurprising that money market and income funds are now attracting the bulk of investor flows.

Longer term investment strategies such as equity and traditional balanced funds have lost out. This is typical investor behaviour, consistent with past cycles. However, it is damaging to long-term investment outcomes because the market mechanism soon ensures that growth assets again offer risk premiums sufficient to attract investors' savings.

One of Foord's key investment tenets is to preserve investors' capital in real terms, that is after subtracting inflation. Further, we aim to achieve returns meaningfully above inflation to compound real capital growth. We believe inflation plus at least 5% per annum over a full investment cycle is achievable without undue risk. As we see from the graph, cash and bonds seldom achieve this outcome over five years. But these asset classes can achieve this goal over shorter time periods and therefore have their place in portfolios.

Achieving long-term inflation-beating returns requires patience. This is especially true when share and bond prices diverge drastically from market fundamentals. Broad investment choice across multiple and uncorrelated asset classes allows the portfolio managers to diversify investment risk while buying low and selling high.

We are not advocating short-term trading or trying to accurately predict a market correction (inflection point). Rather, market timing involves up or down-weighting asset classes based on the relative attractiveness of the market. This approach is based on a thorough analysis of the interest rate cycle which is a key component of all asset prices.

In our long experience, it is better to de-risk investment portfolios well before an expected inflection point as restructuring portfolios can become impossible in a bear market when trading volumes and liquidity dry up. In short, we prefer to leave the dancefloor while the music is still playing.

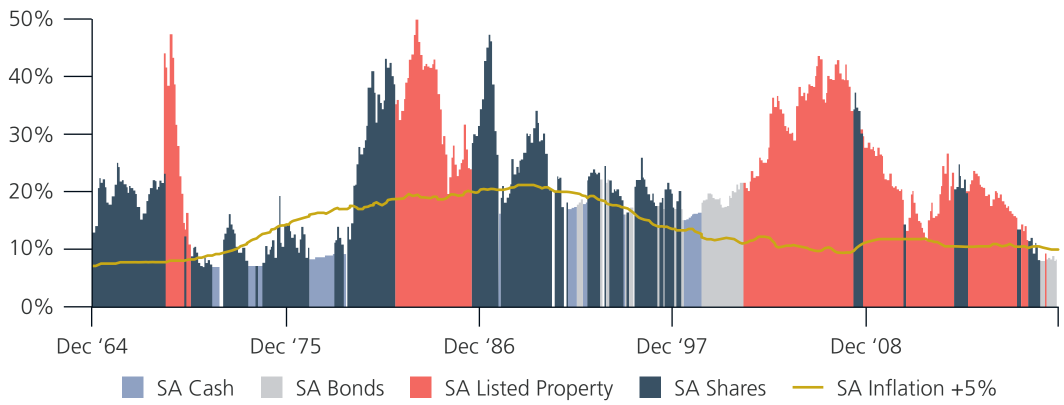
Being early in this way often results in short-term underperformance as other market participants extrapolate recent growth trends into the future. In each event, however, Foord's investors have subsequently enjoyed much longer periods of outperformance.

Preserving capital during market downturns is only one aspect of long-term investment success. Moving early into the safety of cash, government bonds and defensive equities improves portfolio liquidity. This is critical when other investors rush for the exits when the inflection point hits.

Just as asset prices overshoot at market highs, they fall too far in bear markets. This gives us excellent buying opportunities. But investors can only benefit from bargain prices if they have enough liquidity, which is difficult to achieve in a falling market.

Bull markets tend to last much longer than bear markets. Positioning investor portfolios for the next bull market requires liquidity, patience, objective thinking and flexibility. Foord's portfolios are now very well positioned on all four metrics.

ROLLING 5-YEAR ASSET CLASS WINNERS



SIMPLE BUT NOT EASY

KAREN DU TOIT
Head of Retail Investments: North Gauteng

For many of us, investing appears to be a complex field of study with mathematical formulas resembling hieroglyphics. This may be true for a Masters of Finance textbook, but there is another, arguably more important, side to investing. KAREN DU TOIT explores the fuzzy, less mathematical, human behavioural aspect of investing.

The study of investor behaviour or investor psychology is a field that has become increasingly prominent over the last decade. It examines not only finance but also how people behave with money. Behaviour is the way we respond to a particular situation or stimulus. How we behave is in turn affected by our past, our generation, where we live, our personality and circumstances. It is usually emotional and therefore no less complex than the numeric side of investing.

Warren Buffet famously said that investing is simple, but not easy. This may be true if you remove emotions and behavioural biases as the best investors can do. To the rest of us, yoked by fear and greed, there appears to be nothing simple about investing.

When going through times of volatility or underperformance it's very difficult for the lay person to remain disciplined and stick to their investment plan. We are hard wired to eschew immediate pain. We want to escape it, even when rational, objective thinking suggests we are better off in the long term by waiting for the cycle to turn.

We can study investor behaviour by discerning patterns in industry savings statistics. There is a clear pattern of investors switching from the worst performing funds to the best performing funds based on past performance. This is evidence of backward-looking biases and extrapolation of the past into the future. In behavioural finance jargon, this is called extrapolation bias, which is the tendency to overweight recent events when making decisions about the future.

For example, while balanced funds have investment horizons of five or more years, investors often judge these funds on one-year performance compared to their peers. The assumption is that the one-year returns can successfully predict the performance over the next five years. By chasing last year's winner, investors could well be selling the following year's top performing fund. It's a vicious cycle.

We see the same value destroying behaviour between different categories of funds. For example, investors switching their retirement savings from long-term, growth-oriented strategies to short-term, money market or income funds. This is partly explained by extrapolation bias but partly by market timing.

Trying to accurately predict a market inflection point is almost always unsuccessful due to behavioural biases. Greed keeps investors in growth assets too long and fear keeps them in cash assets too long. This "sell low, buy high" phenomenon explains why most investors' long-term returns are way below the average of the funds in which they invest. Churning managers comes at great long-term cost.

The most successful long-term investment strategy for lay investors is to set an investment objective that is realistic and within your budget and emotional range; invest regularly to harness the benefits of rand cost averaging and stay invested through market cycles.

HOW TO INVEST
FOR THE CHILDREN IN YOUR LIFE

ARLENE THOMPSON
Investor Relationship Manager: Direct Investors

Since ancient times, it has been customary to plant a tree when a child is born. The tree is a reminder of the loved one who planted it for her. In modern times where many families are split across the world, planting a tree may not be practical. But as ARLENE THOMPSON explains, seeding an investment account for your child, godchild, grandchild, niece or nephew is easy.

MORE THAN JUST A FINANCIAL INVESTMENT

By seeding an investment account for a young child, you are giving the investment a long time to compound meaningfully. Perhaps to fund a first car? Or for tertiary education?

While the financial rewards are obvious, real value comes in talking to the child about the investment to nurture a lifelong savings habit. Encourage the child to add to the investment with some birthday or pocket money. Matching the child's small contributions is an extra incentive and boost to her investment account. Use your investment statements and *Foreword* newsletters as a reason to talk to your children about investing.

THE FIRST STEPS TO INVEST

Only the child's parent or legal guardian may open an account in the name of a minor (under 18 years). Unless the child is registered for income tax, the parents are taxed on any income accruing from their donation until she reaches maturity. The child legally becomes the full owner of the account on turning 18.

Alternatively, you may decide to open a sub-account in your own Foord unit trust investment designated for a child. In this case, the account holder continues to own and operate the account, but the Foord statements will display the sub-account separately. You can donate the units to an account in the child's name when you are ready. Remember to make provision for this sub-account in your will.

> "While the financial rewards are obvious, real value comes in talking to the child about investment to nurture a lifelong savings habit."

The investment can be in the form of a once-off lumpsum or a monthly debit order commitment. It can of course be added to over time. If the investment is in the child's name, it can only be redeemed into the child's own bank account.

Gifting unit trusts may have capital gains and donations tax consequences for the donor. Please consult your tax practitioner for more information on the tax consequences of donations to minors.

For more information contact the Foord Unit Trusts team on 021 532 6969 or unittrusts@foord.co.za.

MARKETS IN A NUTSHELL

WORLD

EQUITIES

Global equities edged higher, led by US and Japanese bourses — while emerging markets, typically geared to growth and trade, fell on slowing growth fears

BONDS

Developed market government bond yields fell materially on weaker macro data and lower short-term cash yields — German 10-year bond yields are now deep into negative territory

CURRENCIES

Given growth and yield differentials, the US dollar was stronger against the euro — while the pound was lower on rising hard Brexit fears

COMMODITIES

Oil prices fell despite attacks on a Saudi Arabian oil facility, while copper declined and iron ore was sharply lower — but precious metals gained as investors found refuge in uncorrelated assets

ECONOMY

Global growth moderated on the escalating US-Sino trade war, rising hard Brexit risks and rising Middle East geopolitical risks — manufacturing is in a multi-month decline in the main manufacturing economies

MONETARY AND FISCAL POLICY

The US Federal Reserve lowered interest rates by half a percent and stopped rebalancing its balance sheet — while the ECB cut interest rates more deeply into negative territory and pleaded for pan-EU fiscal expansion

SOUTH AFRICA

EQUITIES

The FTSE/JSE Capped All Share Index tracked emerging bourses lower — with resources and financial shares falling most

BONDS

The SA All Bond Index edged higher — SA bonds are the best performing asset class on a year-to-date basis

CURRENCIES

The rand weakened sharply against the US dollar — as global investors sought safe-haven assets at the expense of growth-sensitive emerging markets

ECONOMY

The economy recovered from a very weak first quarter with improvements in mining activity and household consumption — but the rebound is off a low base and probably not sustainable

MONETARY AND FISCAL POLICY

SARB's Monetary Policy Committee lowered the SA repo rate by just a quarter-point to 6.5% in July — suggesting a 2% real rate is appropriate, despite near recessionary conditions and benign inflation

FUND RANGE

BEST INVESTMENT VIEW FUNDS

FOORD FLEXIBLE

Exploiting the benefits of global diversification, the fund aims to provide investors with an after-fee return of 5% per annum above the South African inflation rate.

FOR INVESTORS

- With a moderate risk profile
- Seeking long-term inflation-beating returns over periods exceeding five years
- Requiring a balanced exposure to South African and global investments.

FOORD INTERNATIONAL (US$)

The fund aims to achieve meaningful inflation-beating US$ returns over rolling five-year periods from a conservatively managed portfolio of global investments reflecting Foord's prevailing best investment view.

FOR INVESTORS

- With a moderate risk profile
- Requiring diversification through investments not available in South Africa
- Seeking to hedge rand depreciation.

REGULATION 28 FUNDS

FOORD BALANCED

Managed to comply with the statutory investment limits set for retirement funds in South Africa, the fund aims to grow retirement savings by meaningful, inflation-beating returns over the long term.

FOR INVESTORS

- With a moderate risk profile
- Seeking long-term, inflation-beating returns over periods exceeding five years
- From an SA retirement fund investment product (Reg 28).

FOORD CONSERVATIVE

Managed to comply with the statutory investment limits set for retirement funds in South Africa, the fund aims to provide conservative, medium-term investors with inflation-beating returns over rolling three-year periods.

FOR INVESTORS

- With a conservative risk profile
- Close to or in retirement
- Seeking medium-term, inflation-beating returns over periods of three to five years
- From an SA retirement fund investment product (Reg 28).

SPECIALIST EQUITY FUNDS

FOORD EQUITY

The fund aims to outperform the FTSE/JSE Capped All Share Index over the long term, with lower risk of loss.

FOR INVESTORS

- With a higher risk profile
- Seeking long-term growth over periods exceeding five years
- From a portfolio of JSE-listed equity, commodity and property stocks
- And able to withstand investment volatility in the short to medium term.

FOORD GLOBAL EQUITY (US$)

The fund aims to outperform the MSCI All Country World Net Total Return Index from an actively managed portfolio of global equities, without assuming greater risk.

FOR INVESTORS

- With a higher risk profile
- Requiring diversification through investments not available in South Africa
- Seeking to hedge rand depreciation
- And able to withstand investment volatility in the short to medium term.

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