PRUDENTIAL UNIT TRUSTS QUARTERLY COMMENTARY
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

COMBINED QUARTERLY COMMENTARY

INCOME | MULTI-ASSET | PROPERTY/EQUITY | GLOBAL

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PRUDENTIAL MONEY MARKET FUND
31 MARCH 2017

PRUDENTIAL INVESTMENT MANAGERS

QUARTERLY COMMENTARY

PERFORMANCE

Over the past quarter, the fund delivered a return of 1.95% (gross) versus its benchmark the STeFI Call Deposit Index which returned 1.67%. The average duration of the fund at quarter end was 27 days relative to the 90-day maximum average duration.

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. After 11 weeks of improving conditions (with a strengthening rand and brightening outlooks for inflation, interest rates and growth), the local economy and financial markets were hit by a Cabinet reshuffle replacing the Finance Minister and his Deputy, as well as consequent downgrades of the sovereign credit rating to sub-investment grade by S&P Global and Fitch.

The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy (as contained in the latest Budget) and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors and consumers. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

The immediate impact of these moves saw the rand depreciate about 8% against the US dollar during the last trading week of March (starting from when the Finance Minister was recalled from his UK investor roadshow). This erased most of the good gains recorded by the local currency over the quarter, having begun the quarter at R13.73/US$, appreciated to R12.3/US$ and post the news, jumped to around R13.8/US$ in early April; however, it still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro. Market reaction was not nearly as severe as the sharp sell-off at the time of Nenegate in December 2015.

At the SA Reserve Bank's Monetary Policy Committee (MPC) meeting on 29-30 March, the MPC left the repo rate unchanged at 7.0%, citing an improved inflation outlook and subdued energy prices. GDP growth for Q4 2016 slumped to -0.3% q/q annualised, from an upwardly revised 0.4% q/q annualised in Q3. For 2016 as a whole, the economy grew by 0.3% versus 1.5% in 2015, and growth is expected at 1.1% in 2017.

CPI inflation data moderated to 6.3% y/y in February from 6.6% printed in January – in line with market expectations. Core CPI inflation also decelerated from 5.5% to 5.2%. Food inflation printed 10% y/y– and is expected to have peaked on the back of a deceleration in maize prices from the levels seen in at the start of 2016, although meat prices posted an acceleration of 1.6% over the month.

PPI inflation eased to 5.6% y/y in February from 5.9% y/y in January, mainly attributed to food products, beverages and tobacco products. Month-on-month, PPI came in at 0.6% - on the back of increases recorded in petroleum and chemical products, while meat products also posted a 2.1% gain over the month of February.

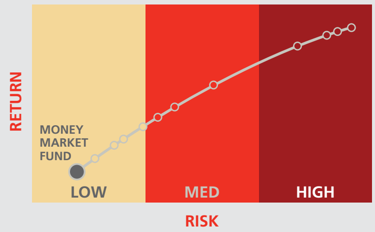
Private sector credit extension (PSCE) moderated to 5.3% y/y for February from 5.5% y/y in January – mainly attributable to the other loans and advances sub-category. Corporates remain a driving factor, with growth in PSCE extended to corporates printing 9.6% y/y. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	X CLASS
1 year	7.5%	7.0%	7.6%
3 years	6.5%	6.2%	6.6%
5 years	6.0%	5.6%	6.1%
7 years	5.9%	5.6%	n/a
10 years	7.1%	6.9%	n/a
Since inception	7.8%	7.7%	6.0%

[#] Inception date X Class: 1 April 2011

INCOME FUND

RISK/RETURN PROFILE:



FUND MANAGERS:

Roshen Harry and Sandile Malinga

ASISA CATEGORY:

South African - Interest Bearing - Money Market

BENCHMARK:

STeFI Call Deposit Index

INCEPTION DATE:

9 April 2002

FUND SIZE:

R2 955 554 005

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL HIGH INTEREST FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

PERFORMANCE

The Prudential High Interest Fund generated a return of 2.36% (gross) for the quarter compared to its benchmark, the STeFI Composite Index, which returned 1.84%.

The Prudential High Interest Fund was launched in December 2010 with the aim of delivering returns in excess of money market yields without compromising the stability of the capital. Although capital protection is not guaranteed we highlight the low-risk nature of the portfolio and hence the remote prospect for capital loss over periods exceeding a few days.

The maximum term of instruments is limited to 3 years compared to money market funds at 13 months. The fund also has a maximum weighted average duration of 180 days as opposed to a typical money market fund targeting a maximum 90-day weighted average maturity.

Relative to the 180-day maximum average duration, the quarter-end duration of the fund came in at 158 days.

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. After 11 weeks of improving conditions (with a strengthening rand and brightening outlooks for inflation, interest rates and growth), the local economy and financial markets were hit by a Cabinet reshuffle replacing the Finance Minister and his Deputy, as well as consequent downgrades of the sovereign credit rating to sub-investment grade by S&P Global and Fitch.

The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy (as contained in the latest Budget) and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors and consumers. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

The immediate impact of these moves saw the rand depreciate about 8% against the US dollar during the last trading week of March (starting from when the Finance Minister was recalled from his UK investor roadshow). This erased most of the good gains recorded by the local currency over the quarter, having begun the quarter at R13.73/US$, appreciated to R12.3/US$ and post the news, jumped to around R13.8/US$ in early April; however, it still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro. Market reaction was not nearly as severe as the sharp sell-off at the time of Nenegate in December 2015.

At the SA Reserve Bank's Monetary Policy Committee (MPC) meeting on 29-30 March, the MPC left the repo rate unchanged at 7.0%, citing an improved inflation outlook and subdued energy prices. GDP growth for Q4 2016 slumped to -0.3% q/q annualised, from an upwardly revised 0.4% q/q annualised in Q3. For 2016 as a whole, the economy grew by 0.3% versus 1.5% in 2015, and growth is expected at 1.1% in 2017.

SA 10-year nominal bond yields rose from around 8.4% (prior to news of the Finance Minister's recall) to around 8.9% on 31 March, before rising above 9% in the first week of April. This also reversed some of the good gains accumulated over the quarter in response to strong foreign investor demand for EM assets. For the quarter, the BEASSA All Bond Index returned 2.5%. As of 17 March, however, it had returned 4.2% for 2017 (over the first 11 weeks of the year). Inflation-linked bonds (ILB Composite Index) lost 0.6% in the quarter as inflation expectations adjusted higher. Cash (the STeFI Composite) returned 1.8%.

FUND STRATEGY

The Fund has generally sought to take advantage of banks' requirements to secure longer dated funding which better matches the profile of their loan books. This has led to a steep credit curve whereby they are prepared to pay significantly more for funding beyond the 12-month point. We prefer these longer-dated securities and have exposure to securities issued by banks such as ABSA, Standard Bank, FirstRand, Nedbank and Investec both in floating and fixed-rate securities.

Exposure to floaters in the 3-year space was increased over the quarter on the back of attractive pricing. Credit issuance has been scarce since early 2016, and while demand to tap into more of that market in order to lock in yield pick-up remains a focus, names we were comfortable investing in at spreads in line with our valuation metrics were limited over the quarter and include the rolling-over of maturing paper.

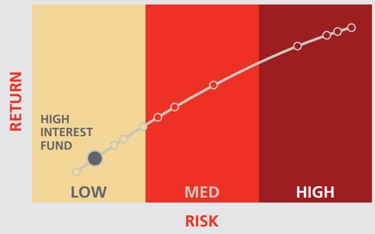
We continue to look for opportunities that will enhance the return to investors without compromising the stability of their capital. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	X CLASS	D CLASS
1 year	8.8%	7.6%	9.0%	9.0%
2 years	7.6%	7.1%	7.8%	7.8%
3 years	7.1%	6.8%	7.2%	7.3%
5 years	6.5%	6.2%	6.6%	6.8%
Since inception	6.3%	6.1%	6.4%	6.7%

Inception dates: X Class: 1 April 2011, D Class: 9 December 2010

INCOME FUND

RISK/RETURN PROFILE:



FUND MANAGERS:
Roshen Harry and Sandile Malinga

ASISA CATEGORY:
South African - Interest Bearing - Short Term

BENCHMARK:
STeFI Composite Index measured over a rolling 12-month period

INCEPTION DATE:
8 December 2010

FUND SIZE:
R6 570 280 579

PLEASE NOTE:
This fund is capped to new investors

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL HIGH YIELD BOND FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

INCOME FUND

PERFORMANCE

For the quarter, the fund returned 2.3% (net of fees) compared to the 2.5% delivered by its benchmark, the BEASSA All Bond Index. It outperformed cash (as measured by the STeFI Composite Index), which returned 1.8%, and inflation-linked bonds at -0.6% (JSE CILI). We started the quarter with the portfolio overweight in duration, and reduced this to a neutral position early in the quarter when bond yields dropped based on a renewed appetite for emerging market bonds. We continue to look for opportunities to add to our corporate bond exposure.

Fund performance benefitted from income accrual over the quarter and the increased yield derived from non-government bonds; the portfolio ended the quarter with a 25% weighting to corporate issuers.

MARKET OVERVIEW

In the US, as in the previous quarter, stronger-than-expected GDP growth (at 2.1% in Q4 2016 q/q annualised) combined with a tighter jobs market, as well as firming inflation, to reinforce the widely expected Fed rate hike of 25bps in March. FOMC members' consensus forecasts indicated a further two 25bp rate hikes in 2017 given the underlying healthy economy. In turn, the interest rate market was also discounting at least another two 25bp increases this year.

The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, managed to return 1.8% in the quarter, reversing some of Q4's sharp losses as 10-year yields of over 2% attracted investors. US investment grade corporate bond spreads versus USTs narrowed only marginally to 122bps from 129bps, while high-yield bond spreads fell by around 37bps (led by telecom and healthcare companies rather than the energy sector this quarter). A slightly weaker US dollar vs the yen and euro also lifted bond returns from these markets.

In the Eurozone, worries of a populist victory in the Netherlands' election were put to rest as the far-right party lost by a sound margin. French elections will be the next test: the anti-euro nationalist party is expected to perform well. The region's Q4 2016 GDP growth was reported steady at 1.8% (q/q annualised), fuelled by the ECB's ongoing easy monetary policy, while inflation picked up to 2% y/y in February, mostly on the back of higher energy costs. Although Britain served its formal "Brexit" notice to the EU in March and its ability to negotiate favourable exit terms appeared increasingly difficult, UK economic data was upbeat. Sterling remained weak, however, spurring more inflation worries for 2017, and the Bank of England refrained from raising interest rates.

In Japan, Q4 2016 GDP growth disappointed slightly at 1.0% q/q annualised from a revised 1.4% in the previous quarter - private consumption was essentially flat while export growth accelerated. The Finance Minister said the economy remained in a "moderate recovery" after four quarters of expansion, with the job market improving. Core inflation also rose to 0.2% y/y in February due to higher energy prices.

In China, 2017 started strongly with the MSCI China posting a total return of 12.9% (in US$) in Q1 – its best start in years – amid improving corporate fundamentals, solid investor demand and low volatility. The yuan's exchange rate stabilised on the back of the improving global trade outlook, and concerns over growth and previous market volatility receded. GDP growth for Q4 2016 was reported at 6.8% (q/q annualised), slightly above the 6.7% expected, as consumer spending accelerated and the property market rebounded. Other emerging market assets, including both bonds and equities, recorded good gains amid renewed investor demand for risk assets.

In South Africa, much has been written about the Cabinet reshuffle and resulting credit rating downgrades by S&P Global (and later Fitch) to sub-investment grade that occurred at the end of March/early April. The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy (as contained in the latest Budget) and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors and consumers. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

The immediate impact of these moves saw the rand depreciate about 8% against the US dollar during the last trading week of March; however, it still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro. Market reaction was not nearly as severe as the sharp sell-off at the time of Nenegate in December 2015.

Meanwhile, SA 10-year nominal bond yields rose from around 8.4% (prior to news of the Finance Minister's recall) to around 8.9% on 31 March, before rising above 9% in the first week of April. This also reversed some of the good gains accumulated over the quarter in response to strong foreign investor demand for EM assets. For the quarter, the BEASSA All Bond Index returned 2.5%. As of 17 March, however, it had returned 4.2% for 2017 (over the first 11 weeks of the year).

At the SA Reserve Bank's Monetary Policy Committee (MPC) meeting on 29-30 March, the MPC left the repo rate unchanged at 7.0%, citing an improved inflation outlook and subdued energy prices. February CPI slowed to 6.3% y/y from 6.6% y/y in January as food prices fell; however, this welcome development was quickly overtaken by the subsequent Cabinet reshuffle and downgrades. GDP growth for Q4 2016 slumped to -0.3% q/q annualised, from an upwardly revised 0.4% q/q annualised in Q3, as mining and manufacturing output shrank. For 2016 as a whole, the economy grew by 0.3% versus 1.5% in 2015, and growth is expected at 1.1% in 2017.

OUTLOOK

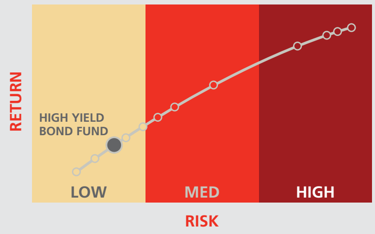
South Africa's new sub-investment grade credit rating status and uncertainty around our fiscal policy implementation, governance standards and political risk will keep financial market volatility elevated in the months ahead. Importantly, the extent of further rand depreciation following the downgrades will determine how much higher inflation and interest rates will rise over the medium term, which in turn would impact on interest-rate-sensitive assets like bonds.

As prudent valuation-based investment managers, we believe there will be opportunities created by the greater uncertainty now prevailing that could allow us to buy assets at attractive valuations where the risks are appropriate. This will benefit clients over the medium to long term. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	10.9%	11.0%	11.3%
3 years	6.4%	7.5%	6.9%
5 years	6.9%	7.4%	7.2%
7 years	8.2%	8.3%	8.5%
10 years	7.8%	8.1%	8.2%
Since inception	10.3%	10.5%	9.2%

Inception date B Class: 1 April 2003

RISK/RETURN PROFILE:



FUND MANAGERS:

David Knee and Gareth Bern

ASISA CATEGORY:

South African - Interest Bearing - Variable Term

BENCHMARK:

BEASSA Total Return All Bond Index

INCEPTION DATE:

27 October 2000

FUND SIZE:

R503 343 953

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Sources: Prudential, Morningstar & Deutsche Securities

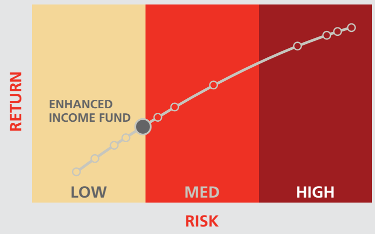
PRUDENTIAL ENHANCED INCOME FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

RISK/RETURN PROFILE:



FUND MANAGERS:
David Knee and Roshen Harry

ASISA CATEGORY:
South African - Multi-Asset - Income

BENCHMARK:
STeFI Composite Index measured over a rolling 36-month period

INCEPTION DATE:
1 July 2009

FUND SIZE:
R2 243 079 772

PERFORMANCE

For the three months ending 31 March 2017 the fund returned 2.3% (net of fees), beating the 1.8% returned by its benchmark, the STeFi composite index. Over a one-year period the fund delivered 8.9% (net of fees), outperforming its benchmark by 1.3%.

Among the largest contributors to performance over the quarter in absolute terms were the fund's holdings of SA nominal bonds (with a weighting of 32% of the fund) and cash (mainly comprising floating-rate notes and money market instruments), as well as international bonds. International equity exposure also contributed positively, despite the rand's appreciation over the three months. The fund's total international exposure currently stands at 15%.

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China experienced one of its strongest starts to a year in equities, helped by low market volatility and improving economic and corporate fundamentals. By contrast, in South Africa, after 11 weeks of improving conditions (with a strengthening rand and brightening outlooks for inflation, interest rates and growth), the local economy and financial markets were hit by a Cabinet reshuffle replacing the Finance Minister and his Deputy, as well as consequent downgrades of the sovereign credit rating to sub-investment grade by S&P Global and Fitch.

In the US, as in the previous quarter, stronger-than-expected GDP growth (at 2.1% in Q4 2016 q/q annualised) combined with a tighter jobs market, as well as firming inflation, to reinforce the widely expected Fed rate hike of 25bps in March. FOMC members' consensus forecasts indicated a further two 25bp rate hikes in 2017 given the underlying healthy economy. In turn, the interest rate market was also discounting at least another two 25bp increases this year.

The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, managed to return 1.8% in the quarter, reversing some of Q4's sharp losses as 10-year yields of over 2% attracted investors. US investment grade corporate bond spreads versus USTs narrowed only marginally to 122bps from 129bps, while high-yield bond spreads fell by around 37bps (led by telecom and healthcare companies rather than the energy sector this quarter). A slightly weaker US dollar vs the yen and euro also lifted bond returns from these markets. In the equity market, stocks rallied strongly, boosted by hopes of higher government spending, corporate tax cuts and deregulation under Trump: the S&P 500 returned 6.1%, the Dow Jones 5.2% and the Nasdaq 12.1% for the quarter.

In the Eurozone, worries of a populist victory in the Netherlands' election were put to rest as the far-right party lost by a sound margin. French elections will be the next test: the anti-euro nationalist party is expected to perform well. The region's Q4 2016 GDP growth was reported steady at 1.8% (q/q annualised), fuelled by the ECB's ongoing easy monetary policy, while inflation picked up to 2% y/y in February, mostly on the back of higher energy costs. The Dow Jones Eurostoxx 50 returned 8.3%, while Germany's DAX returned 8.8% and the French CAC 7.1% (all in US$). Although Britain served its formal "Brexit" notice to the EU in March and its ability to negotiate favourable exit terms appeared increasingly difficult, UK economic data was upbeat and the FTSE 100 returned 5.3% (in US$) over the quarter. Sterling remained weak, however, spurring more inflation worries for 2017, and the Bank of England refrained from raising interest rates.

In China, 2017 started strongly with the MSCI China posting a total return of 12.9% (in US$) in Q1 – its best start in years – amid improving corporate fundamentals, solid investor demand and low volatility. The yuan's exchange rate stabilised on the back of the improving global trade outlook, and concerns over growth and previous market volatility receded. GDP growth for Q4 2016 was reported at 6.8% (q/q annualised), slightly above the 6.7% expected, as consumer spending accelerated and the property market rebounded.

Other emerging market assets, including both bonds and equities, recorded good gains amid renewed investor demand for risk assets. Overall, the MSCI Emerging Markets Index returned an impressive 11.4% in US$, compared to 6.4% from the MSCI World Free Index for developed markets. The MSCI India was the strongest performer with a 17.1% total return over the quarter, followed by South Korea's KOSPI (+16.5%), the MSCI China (+12.9%), Brazil's Bovespa (+11%) and the MSCI Turkey (+10.9%) all in US$. The MSCI South Africa returned 4.6% for Q1 in US$.

In commodities, the oil price softened somewhat to trade around US$50/barrel at quarter-end from around $55 at the start of the year as the effects of a curtailed supply stemming from the OPEC agreement were offset to some extent by rising supplies from the US. Brent crude fell 7.0% over the quarter. Most other commodity prices were firmer, however, on signs of improving global growth and re-emerging inflationary pressures. Gold gained 8.9% in Q1, while platinum rose 5.2% and palladium was up 19.1%. Other good gains were recorded by aluminium (+14.6%), lead (+16.6%) and zinc (+7.5%).

Much has been written about South Africa's Cabinet reshuffle and resulting credit rating downgrades by S&P Global (and later Fitch) to sub-investment grade that occurred at the end of March/early April. The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy (as contained in the latest Budget) and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors and consumers. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

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Meanwhile, SA 10-year nominal bond yields rose from around 8.4% (prior to news of the Finance Minister's recall) to around 8.9% on 31 March, before rising above 9% in the first week of April. For the quarter, the BEASSA All Bond Index returned 2.5%. Inflation-linked bonds (ILB Composite Index) lost 0.6% in the quarter as inflation expectations adjusted higher, while Listed property was also sold off in late March as an interest-rate-sensitive asset, but managed to return 1.4% in Q1. Cash (the STeFI Composite) returned 1.8%.

At the SA Reserve Bank's Monetary Policy Committee (MPC) meeting on 29-30 March, the MPC left the repo rate unchanged at 7.0%, citing an improved inflation outlook and subdued energy prices. February CPI slowed to 6.3% y/y from 6.6% y/y in January as food prices fell; however, this welcome development was quickly overtaken by the subsequent Cabinet reshuffle and downgrades. GDP growth for Q4 2016 slumped to -0.3% q/q annualised, from an upwardly revised 0.4% q/q annualised in Q3, as mining and manufacturing output shrank. For 2016 as a whole, the economy grew by 0.3% versus 1.5% in 2015, and growth is expected at 1.1% in 2017.

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	X CLASS	D CLASS
1 year	8.9%	7.6%	9.4%	9.1%	9.5%
3 years	7.5%	7.2%	n/a	7.7%	8.1%
5 years	7.8%	6.6%	n/a	8.1%	8.4%
7 years	8.4%	7.1%	n/a	n/a	n/a
Since inception	8.6%	7.3%	7.3%	8.3%	8.6%

Inception dates: X Class: 1 April 2011, D Class: 1 July 2011, T Class: 2 January 2015

Sources: Prudential, Morningstar & Deutsche Securities

STRATEGY AND OUTLOOK

In global fixed income, although government bond yields have stayed on a rising trend, especially in the US (with the yield on the 10-year US Treasury bond at around 2.42% at quarter-end), they continue to be expensive given the very low base from which they started.

For global equities, the ongoing rally in many global equity markets (especially the US) has kept valuations at levels more expensive than those of South Africa, on the basis of both 12-month forward P/E and price-to book measures. Our exposures in the fund are concentrated in European markets where long-standing growth concerns have kept valuations on the cheap side of fair value. Over the quarter equity risk premiums (the yield on equities vs bonds) narrowed, but still provide a substantial valuation buffer that should help to protect equities in the event of growth disappointment.

In SA listed property, we have maintained our exposure in the fund, with yields at even more attractive levels following the late March/early April sell-off. At quarter-end, listed property companies (excluding developers) were priced to return approximately 16% p.a. over the medium-term (assuming no change in the market's valuation of property), comfortably above inflation and, we believe, ample compensation for the risk involved.

In SA nominal bonds, we took some profits in mid-March (before the sell-off) when prices had rallied to reach attractive levels, trimming our moderately overweight position.

Inflation-linked bonds remained somewhat expensive compared to conventional bonds over the quarter, leading us to favour SA nominal bonds. The 10-year break-even inflation rate fell to a low of around 6.3% in mid-March before jumping to 6.5% at month-end, lower than the 6.8% seen in the previous quarter, but still elevated compared to our long-term inflation benchmark of 6.0%.

Looking ahead, South Africa's new sub-investment grade credit rating status and uncertainty around our fiscal policy implementation, governance standards and political risk will keep financial market volatility elevated in the months ahead. Importantly, the extent of further rand depreciation following the downgrades will determine how much higher inflation and interest rates will rise over the medium term, which in turn would impact on interest-rate-sensitive assets like bonds and listed property.

As prudent valuation-based investment managers, we believe there will be opportunities created by the greater uncertainty now prevailing that could allow us to buy assets at attractive valuations where the risks are appropriate. This will benefit clients over the medium to long term. Having recently reduced our bond exposure as the market rallied, for example, these setbacks have presented an opportunity to reacquire some of those securities at significantly lower prices. ■

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL INFLATION PLUS FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China experienced one of its strongest starts to a year in equities, helped by low market volatility and improving economic and corporate fundamentals. By contrast, in South Africa, after 11 weeks of improving conditions (with a strengthening rand and brightening outlooks for inflation, interest rates and growth), the local economy and financial markets were hit by a Cabinet reshuffle replacing the Finance Minister and his Deputy, leading to downgrades of the sovereign credit rating to sub-investment grade by S&P Global and Fitch.

US reflation trend continues as global prospects improve

In the US, as in the previous quarter, stronger-than-expected GDP growth combined with a tighter jobs market, as well as firming inflation, to reinforce the widely expected Fed rate hike of 25bps in March. FOMC members' consensus forecasts indicated a further two 25bp rate hikes in 2017 given the underlying healthy economy.

The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, managed to return 1.8% in the quarter, reversing some of Q4's sharp losses as 10-year yields of over 2% attracted investors. In the equity market, stocks rallied strongly, boosted by hopes of higher government spending, corporate tax cuts and deregulation under Trump: the S&P 500 returned 6.1% and the Nasdaq 12.1% for the quarter. In the Eurozone and UK, similar conditions saw the Dow Jones Eurostoxx 50 return 8.3%, while Germany's DAX returned 8.8%, the French CAC 7.1% and the FTSE 100 5.3% (all in US$). Finally, the Nikkei 225 Index returned 4.5% (in US$).

The MSCI China posted a total return of 12.9% (in US$) in Q1 – its best start in years – amid improving corporate fundamentals, solid investor demand and low volatility. GDP growth for Q4 2016 was reported at 6.8% (q/q annualised), slightly above the 6.7% expected, as consumer spending accelerated and the property market rebounded. Other emerging market assets, including both bonds and equities, recorded good gains amid renewed investor demand for risk assets. Overall, the MSCI Emerging Markets Index returned an impressive 11.4% in US$, compared to 6.4% from the MSCI World Free Index for developed markets.

In South Africa, much has been written about the Cabinet reshuffle and resulting credit rating downgrades by S&P Global (and later Fitch) to sub-investment grade that occurred at the end of March/ early April. The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

The immediate impact of these moves saw the rand depreciate about 8% against the US dollar during the last trading week of March; however, the local currency still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro. Meanwhile, SA 10-year nominal bond yields rose from around 8.4% (prior to news of the Finance Minister's recall) to around 8.9% on 31 March, before rising above 9% in the first week of April. For the quarter, the BEASSA All Bond Index returned 2.5%. Inflation-linked bonds (ILB Composite Index) lost 0.6% in the quarter as inflation expectations adjusted higher. Cash (the STeFI Composite) returned 1.8%.

Equities were the top performing local asset class for the quarter, with the FTSE/JSE All Share Index returning 3.8%. This reflected a relatively strong performance from industrial counters (+6.6%) given their rand-hedge characteristics, and resources (+2.7%) as commodity prices continued to rise. Financials (particularly banking shares) were hardest hit by the turmoil with a total return of -1.1% over the three months, and retailers' shares were also sold off given the bleaker prospects for consumer wallets. Listed property was also sold off in late March as an interest-rate-sensitive asset, but managed to return 1.4% in Q1.

PERFORMANCE

The fund returned 1.7% (net of fees) for the first quarter of 2016 and has returned 3.1% for the 12-month period ending 31 March 2017. The fund has delivered a return of 12.9% per annum since inception (net of fees), while CPI inflation has averaged 5.8% per annum over the same period. To 31 March 2017 it retains its top-quartile or better performance over annual periods from 3-10 years, according to Morningstar. The largest contributors to absolute returns for the quarter were the fund's holdings in SA and international equities, with notable contributions from its exposure to large global stocks like Naspers, BAT and Richemont. Detracting from value were financial shares like Barclays Group Africa and FirstRand, as well as the overweight in Netcare. Overweight holdings in local nominal bonds and listed property also added value. On a relative basis, as in the previous two quarters, it was the underweight holdings in international fixed income that added the most relative value to returns, followed by international equity exposure. The overweight holdings in SA nominal bonds and equities (to a lesser extent) also added relative value, as did the underweight in ILBs.

STRATEGY AND OUTLOOK

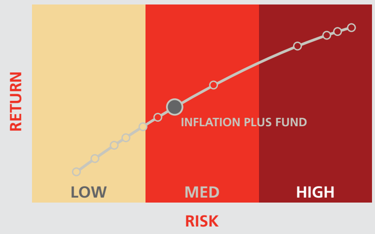
In global fixed income, although government bond yields have stayed on a rising trend, especially in the US (with the yield on the 10-year US Treasury bond at around 2.42% at quarter-end), they continue to be expensive given the very low base from which they started. We remain underweight sovereign bonds and underweight duration, and continue to hold cash and shorter-term bonds in order to reduce interest rate risk. We are neutral on both investment-grade and high-yield corporate bonds in the US and Europe, as corporate spreads versus USTs have narrowed to be largely priced at fair value to slightly expensive.

For global equities, the ongoing rally in many global equity markets (especially the US) has kept valuations at levels more expensive than those of South Africa, on the basis of both 12-month forward P/E and price-to book measures. As such, we have retained our neutral positioning in global equities. Over the quarter equity risk premiums (the yield on equities vs bonds) narrowed, but still provide a substantial valuation buffer that should help to protect equities in the event of growth disappointment.

ANNUALISED PERFORMANCE	A CLASS	OBJECTIVE	T CLASS	X CLASS	B CLASS
1 year	3.1%	11.3%	3.6%	3.3%	3.8%
3 years	7.9%	10.7%	n/a	8.2%	8.7%
5 years	11.3%	10.8%	n/a	11.5%	12.1%
7 years	11.3%	10.5%	n/a	n/a	12.1%
10 years	10.1%	11.6%	n/a	n/a	10.8%
Since inception	13.0%	11.3%	5.6%	11.9%	13.0%

[#] Inception dates: X Class: 1 July 2011, B Class: 1 July 2002, T Class: 2 January 2015

RISK/RETURN PROFILE:



FUND MANAGERS:
Michael Moyle, David Knee, Duncan Schwulst and Johny Lambridis

ASISA CATEGORY:
South African - Multi-Asset - Low Equity

OBJECTIVE:
CPI+5% p.a. over a rolling 3-year period

INCEPTION DATE:
1 June 2001

FUND SIZE:
R37 789 444 481

AWARDS:
Raging Bull: 2013
Morningstar: 2015

Sources: Prudential, Morningstar & Deutsche Securities

South African equities moved to somewhat more expensive valuations over the quarter compared to their long-term fair value, with the FTSE/JSE ALSI 12-month forward P/E rising to 14.1x at quarter-end from 13.8x in Q4 2016. Earnings growth improved largely on the back of higher earnings from resource companies (due to rising commodity prices), while earnings from financial and industrial stocks tracked sideways. Share price increases outpaced earnings growth, however. In the fund we continue to be overweight in local equities on an asset allocation basis.

Rand hedge stocks have benefitted from the state of heightened uncertainty, and should continue to do so in the short term. The fund is overweight stocks like Naspers, British American Tobacco, Exxaro, Sasol, Anglo American and Glencore. We also hold non-mining stocks like Sappi. We have also been overweight in Financials, although we pared our overweight position in the sector prior to the downgrade: our ongoing overweights include Old Mutual and Barclays Group Africa. We have been underweight in Retailers given the challenging consumer environment, but do continue to hold selective overweights in Foschini and Pick 'n Pay.

In SA listed property, we have maintained our overweight exposure in the fund, with yields at even more attractive levels following the late March/early April sell-off. At quarter-end, listed property companies (excluding developers) were priced to return approximately 16% p.a. over the medium-term (assuming no change in the market's valuation of property), comfortably above inflation and, we believe, ample compensation for the risk involved.

In SA nominal bonds, we took some profits in mid-March (before the sell-off) when prices had rallied to reach attractive levels, trimming our moderately overweight position. However, we subsequently bought back part of this holding as yields rose following the sell-off, with the 10-year government bond trading above 9.0%. Consequently, we are still modestly overweight bonds in the fund. Within this exposure, we are also overweight longer-dated bonds versus shorter paper due to the more attractive yields on offer, while retaining our overweight exposure to corporate bonds.

Inflation-linked bonds remained somewhat expensive compared to conventional bonds over the quarter, leading us to maintain our underweight in these assets in favour of SA equities, listed property and nominal bonds. The 10-year break-even inflation rate fell to a low of around 6.3% in mid-March before jumping to 6.5% at month-end, lower than the 6.8% seen in the previous quarter, but still elevated compared to our long-term inflation benchmark of 6.0%.

LOOKING AHEAD

South Africa's new sub-investment grade credit rating status and uncertainty around our fiscal policy implementation, governance standards and political risk will keep financial market volatility elevated in the months ahead. Importantly, the extent of further rand depreciation following the downgrades will determine how much higher inflation and interest rates will rise over the medium term, which in turn would impact on interest-rate-sensitive assets like bonds and listed property. As prudent valuation-based investment managers, we believe there will be opportunities created by the greater uncertainty now prevailing that could allow us to buy assets at attractive valuations where the risks are appropriate. This will benefit clients over the medium to long term. Having recently reduced our bond exposure as the market rallied, for example, these setbacks have presented an opportunity to reacquire some of those securities at significantly lower prices. ■

ASSET CLASS RETURNS IN RANDS	Q1 2017	YTD
SA Equity (FTSE/JSE All Share Index)	3.8%	3.8%
SA Property (FTSE/JSE SA Listed property Index)	1.4%	1.4%
SA Bonds (BEASSA All Bond Index)	2.5%	2.5%
SA Inflation-linked Bonds (RSA Composite Inflation-linked Bond Index)	-0.5%	-0.5%
SA Cash (STeFI Composite)	1.8%	1.8%
Global Equity (MSCI World Free Index - US$)	6.5%	6.5%
Global Equity (MSCI Emerging Markets Index – US$)	11.4%	11.4%
Global Bonds (Barclays Global Aggregate Bond Index – US$)	1.8%	1.8%
Rand (Rand/USD move)	-2.2%	-2.2%

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL BALANCED FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

PERFORMANCE

The Fund's return was slightly positive over the quarter. The main contributors were the positive returns from domestic and international equities. The improved view of the outlook for growth under a Trump Presidency continued to lift spirits, pushing equity markets still higher, while growth in the UK and Europe bolstered markets there. Domestic bonds also contributed favourably as it was one of the stronger performing local asset class. The main contributor to the Fund's performance relative to the market, was its strong returns from international equity stock selection that led to outperformance over the MSCI AC World Index. Other contributors were the Fund's holding of short dated global high yield bonds and international cash that outperformed their respective benchmark indices. The overweight position in local fixed income securities also contributed as a favourable tailwind from improving inflation and international investor sentiment outweighed the negative implications from a change in Finance Minister at the end of the quarter.

MARKET OVERVIEW

The first quarter of 2017 saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China experienced one of its strongest starts to a year in equities, helped by low market volatility and improving economic and corporate fundamentals. By contrast, in South Africa, after 11 weeks of improving conditions (with a strengthening rand and brightening outlooks for inflation, interest rates and growth), the local economy and financial markets were hit by a Cabinet reshuffle replacing the Finance Minister and his Deputy, as well as consequent downgrades of the sovereign credit rating to sub-investment grade by S&P Global and Fitch.

In the US, as in the previous quarter, stronger-than-expected GDP growth combined with a tighter jobs market, as well as firming inflation, reinforced the widely expected Fed rate hike of 25bps in March. The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, managed to return 1.8% in the quarter, reversing some of Q4's sharp losses as 10-year yields of over 2% attracted investors. US investment grade corporate bond spreads versus USTs narrowed only marginally to 122bps from 129bps, while high-yield bond spreads fell by around 37bps (led by telecom and healthcare companies rather than the energy sector this quarter). A slightly weaker US dollar vs the yen and euro also lifted bond returns from these markets. In the equity market, stocks rallied strongly, boosted by hopes of higher government spending, corporate tax cuts and deregulation under Trump: the S&P 500 returned 6.1%, the Dow Jones 5.2% and the Nasdaq 12.1% for the quarter.

In the Eurozone, Q4 2016 GDP growth was reported steady at 1.8% (q/q annualised), fuelled by the ECB's ongoing easy monetary policy, while inflation picked up to 2% y/y in February, mostly on the back of higher energy costs. The Dow Jones Eurostoxx 50 returned 8.3%, while Germany's DAX returned 8.8% and the French CAC 7.1% (all in US$). Although Britain served its formal "Brexit" notice to the EU in March and its ability to negotiate favourable exit terms appeared increasingly difficult, UK economic data was upbeat and the FTSE 100 returned 5.3% (in US$) over the quarter. Sterling remained weak, however, spurring more inflation worries for 2017, and the Bank of England refrained from raising interest rates.

In Japan, Q4 2016 GDP growth disappointed slightly at 1.0% q/q annualised. The Nikkei 225 Index returned 4.5% over the quarter (in US$). The MSCI China posted a total return of 12.9% (in US$) in Q1 amid improving corporate fundamentals, solid investor demand and low volatility. The yuan's exchange rate stabilised on the back of the improving global trade outlook, and concerns over growth and previous market volatility receded. GDP growth for Q4 2016 was reported at 6.8% (q/q annualised). Other emerging market assets, including both bonds and equities, recorded good gains amid renewed investor demand for risk assets. Overall, the MSCI Emerging Markets Index returned an impressive 11.4% in US$, compared to 6.4% from the MSCI World Free Index for developed markets.

In commodities, the oil price softened somewhat to trade around US$50/barrel at quarter-end from around $55 at the start of the year as the effects of a curtailed supply stemming from the OPEC agreement were offset to some extent by rising supplies from the US. Brent crude fell 7.0% over the quarter. Most other commodity prices were firmer, however, on signs of improving global growth and re-emerging inflationary pressures. Gold gained 8.9% in Q1, while platinum rose 5.2% and palladium was up 19.1%.

Locally, much has been written about the Cabinet reshuffle and resulting credit rating downgrades by S&P Global (and later Fitch) to sub-investment grade that occurred at the end of March/early April. The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy (as contained in the latest Budget) and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors and consumers. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

The immediate impact of these moves saw the rand depreciate about 8% against the US dollar during the last trading week of March (starting from when the Finance Minister was recalled from his UK investor roadshow). This erased most of the good gains recorded by the local currency over the quarter, having begun the quarter at R13.73/US$, appreciated to R12.3/US$ and post the news, jumped to around R13.8/US$ in early April; however, it still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro. Market reaction was not nearly as severe as the sharp sell-off at the time of Nenegate in December 2015.

Meanwhile, SA 10-year nominal bond yields rose from around 8.4% (prior to news of the Finance Minister's recall) to around 8.9% on 31 March, before rising above 9% in the first week of April. This also reversed some of the good gains accumulated over the quarter in response to strong foreign investor demand for EM assets. For the quarter, the BEASSA All Bond Index returned 2.5%. As of 17 March, however, it had returned 4.2% for 2017 (over the first 11 weeks of the year). Inflation-linked bonds (ILB Composite Index) lost 0.6% in the quarter as inflation expectations adjusted higher. Cash (the STeFI Composite) returned 1.8%.

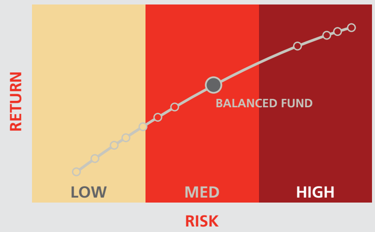
Equities were the top performing local asset class for the quarter, with the FTSE/JSE All Share Index returning 3.8%. This reflected a relatively strong performance from industrial counters (+6.6%) given their rand-hedge characteristics, and resources (+2.7%) as commodity prices continued to rise. Financials (particularly banking shares) were hardest hit by the turmoil with a total return of -1.1% over the three months. Listed property was also sold off in late March as an interest-rate-sensitive asset, but managed to return 1.4% in Q1.

At the SA Reserve Bank's Monetary Policy Committee (MPC) meeting on 29-30 March, the MPC left the repo rate unchanged at 7.0%, citing an improved inflation outlook and subdued energy prices. February CPI slowed to 6.3% y/y from 6.6% y/y in January as food prices fell; however, this welcome development was quickly overtaken by the subsequent Cabinet reshuffle and downgrades. GDP growth for Q4 2016 slumped to -0.3% q/q annualised, from an upwardly revised 0.4% q/q annualised in Q3, as mining and manufacturing output shrank. For 2016 as a whole, the economy grew by 0.3% versus 1.5% in 2015, and growth is expected at 1.1% in 2017.

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	X CLASS	B CLASS
1 year	4.1%	2.2%	4.6%	4.2%	4.8%
3 years	7.9%	6.2%	n/a	8.2%	8.7%
5 years	12.8%	10.0%	n/a	n/a	13.6%
7 years	12.1%	9.7%	n/a	n/a	13.1%
10 years	9.9%	8.1%	n/a	n/a	10.9%
Since inception	14.3%	12.4%	5.5%	11.7%	14.7%

Inception dates: X Class: 2 January 2013, B Class: 1 July 2002, T Class: 2 January 2015

RISK/RETURN PROFILE:



FUND MANAGERS:
David Knee, Duncan Schwulst, Michael Moyle and Johny Lambridis

ASISA CATEGORY:
South African - Multi-Asset - High Equity

BENCHMARK:
ASISA South African - Multi-Asset - High Equity Category Average

INCEPTION DATE:
2 August 1999

FUND SIZE:
R15 698 297 538

Sources: Prudential, Morningstar & Deutsche Securities

PORTFOLIO MANAGER COMMENTS

Global sovereign bond yields continue to be expensive, and we believe investors will likely be disappointed by returns going forward, particularly in a global environment of rising interest rates. We remain underweight sovereign bonds and underweight duration, and continue to hold cash and shorter-term bonds in order to reduce interest rate risk. We are neutral on both investment-grade and high-yield corporate bonds in the US and Europe, as corporate spreads versus USTs have narrowed to be largely priced at fair value to slightly expensive.

For global equities, the ongoing rally in many global equity markets (especially the US) has kept valuations at levels more expensive than those of South Africa, on the basis of both 12-month forward P/E and price-to book measures. In the US, equity prices rose slightly more than earnings growth. As such, we have retained our neutral positioning in global equities in our portfolios as markets remain generally fairly priced, and are underweight global bonds to global cash. Our overweight exposures are concentrated in European markets where long-standing growth concerns have kept valuations on the cheap side of fair value, as well as selected emerging markets including India, funded by underweights in the US, Japan and a variety of other smaller markets including Australia. Over the quarter equity risk premiums (the yield on equities vs bonds) narrowed, but still provide a substantial valuation buffer that should help to protect equities in the event of growth disappointment.

South African equities moved to somewhat more expensive valuations over the quarter compared to their long-term fair value, with the FTSE/JSE ALSI 12-month forward P/E rising to 14.1x at quarter-end from 13.8x in Q4 2016. Earnings growth improved largely on the back of higher earnings from resource companies (due to rising commodity prices), while earnings from financial and industrial stocks tracked sideways. Share price increases outpaced earnings growth, however. The Fund continues to be overweight in local equities on an asset allocation basis.

Rand hedge stocks have benefitted from the state of heightened uncertainty, and should continue to do so in the short term. Prudential's portfolios are overweight stocks like Naspers, British American Tobacco, Exxaro, Sasol, Anglo American and Glencore. We also hold non-mining stocks like Sappi. We have also been overweight in Financials, although we pared our overweight position in the sector prior to the downgrade: our ongoing overweights include Old Mutual, Investec and Barclays Group Africa. We have been underweight in Retailers given the challenging consumer environment, but do continue to hold selective overweights in Foschini and Pick 'n Pay. We have preferred to gain our consumer exposure via well-priced and more defensive consumer services providers like Sun International.

In SA listed property, the Fund has maintained its overweight exposure, with yields at even more attractive levels following the late March/early April sell-off. At quarter-end, listed property companies (excluding developers) were priced to return approximately 16% p.a. over the medium-term (assuming no change in the market's valuation of property), comfortably above inflation and, we believe, ample compensation for the risk involved.

In SA nominal bonds, we took some profits in mid-March (before the sell-off) when prices had rallied to reach attractive levels, trimming our moderately overweight position. However, we subsequently bought back part of this holding as yields rose following the sell-off, with the 10-year government bond trading above 9.0%. Consequently, the Fund is still overweight bonds. Within this exposure, we are also overweight longer-dated bonds versus shorter paper due to the more attractive yields on offer, while retaining our overweight exposure to corporate bonds.

Inflation-linked bonds remained somewhat expensive compared to conventional bonds over the quarter, leading us to maintain our underweight in these assets in favour of SA equities, listed property and nominal bonds. The 10-year break-even inflation rate fell to a low of around 6.3% in mid-March before jumping to 6.5% at month-end, lower than the 6.8% seen in the previous quarter, but still elevated compared to our long-term inflation benchmark of 6.0%.

In SA nominal bonds, we added to our modestly overweight positioning in our multi-asset funds during the quarter following the Trump-related sell-off in the local bond market, given the good value on offer. Our multi-asset portfolios have benefitted from our generally overweight bond positioning during the year. Within this, we are also overweight longer-dated bonds versus shorter paper due to the more attractive yields on offer, while retaining our overweight exposure to corporate bonds. With South Africa's interest rate and inflation outlooks improving, risks to bonds and listed property have moderated somewhat, although the possibility of a credit rating downgrade in 2017 is still a real threat. While SA bond spreads have continued to narrow versus USTs, yields are still pricing in an elevated risk premium.

Inflation-linked bonds remained somewhat expensive compared to conventional bonds over the quarter, leading us to maintain our underweight in these assets in our multi-asset portfolios. The 10-year break-even inflation rate remained around 6.8%, still elevated compared to our long-term inflation benchmark of 6.0%.

LOOKING FORWARD

South Africa's new sub-investment grade credit rating status and uncertainty around our fiscal policy implementation, governance standards and political risk will keep financial market volatility elevated in the months ahead. Importantly, the extent of further rand depreciation following the downgrades will determine how much higher inflation and interest rates will rise over the medium term, which in turn would impact on interest-rate-sensitive assets like bonds and listed property.

As prudent valuation-based investment managers, we believe there will be opportunities created by the greater uncertainty now prevailing that could allow us to buy assets at attractive valuations where the risks are appropriate. This will benefit clients over the medium to long term. Having recently reduced our bond exposure as the market rallied, for example, these setbacks have presented an opportunity to reacquire some of those securities at significantly lower prices. ■

ASSET CLASS RETURNS IN RANDS	Q1 2017	YTD
SA Equity (FTSE/JSE All Share Index)	3.8%	3.8%
SA Property (FTSE/JSE SA Listed property Index)	1.4%	1.4%
SA Bonds (BEASSA All Bond Index)	2.5%	2.5%
SA Inflation-linked Bonds (RSA Composite Inflation-linked Bond Index)	-0.5%	-0.5%
SA Cash (STeFI Composite)	1.8%	1.8%
Global Equity (MSCI World Free Index - US$)	6.5%	6.5%
Global Equity (MSCI Emerging Markets Index – US$)	11.4%	11.4%
Global Bonds (Barclays Global Aggregate Bond Index – US$)	1.8%	1.8%
Rand (Rand/USD move)	-2.2%	-2.2%

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL ENHANCED SA PROPERTY TRACKER FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

PROPERTY

PERFORMANCE

The fund recorded a positive return of 1.7% (net of fees) for the quarter, outperforming its benchmark, the SA Listed Property (SAPY) index, which increased by 1.4%. The fund's 0.3% outperformance versus the benchmark over this period is largely attributable to the active stock selection of our fundamental strategy of holding overweight positions in higher-yielding stocks.

Over the past year the fund returned 2.35% (net of fees), outperforming the benchmark by 0.9%. The rolling 12-month performance of the fund ranked it 15th out of 39 funds in the ASISA South African Real Estate General peer group.

The 10-year track record of the fund ranks it 3rd out of its peers, with the fund having outperformed the benchmark (after fees) over this period.

MARKET COMMENTARY

Internationally the first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets.

In the US, the trend continued, pushing markets still higher. As in the previous quarter, stronger-than-expected GDP growth (at 2.1% in Q4 2016 q/q annualised) combined with a tighter jobs market, as well as firming inflation, to reinforce the widely expected Fed rate hike of 25bps in March. FOMC members' consensus forecasts indicated a further two 25bp rate hikes in 2017 given the underlying healthy economy. In turn, the interest rate market was also discounting at least another two 25bp increases this year. At the same time, surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China improving economic and corporate fundamentals.

By contrast, in South Africa, after experiencing of improving conditions (with a strengthening rand and brightening outlooks for inflation, interest rates and growth), the local economy and financial markets were hit by a Cabinet reshuffle replacing the Finance Minister and his Deputy, as well as consequent downgrades of the sovereign credit rating to sub-investment grade by S&P Global and Fitch at the end of March/early April.

The appointment of an inexperienced leadership team at National Treasury without a solid reputation for fiscal probity has undermined confidence in the Treasury's ability to implement sound fiscal policy (as contained in the latest Budget) and reforms, as well as to maintain high standards of governance. This, in turn, has caused heightened political risk and uncertainty among investors and consumers. The sovereign downgrade will lead to higher overseas borrowing costs for both government and SA banks. Fortunately these foreign borrowings are not at high levels by global standards, and therefore for now the impact is relatively muted.

The immediate impact of these moves saw the rand depreciate about 8% against the US dollar during the last trading week of March (starting from when the Finance Minister was recalled from his UK investor roadshow). This erased most of the good gains recorded by the local currency over the quarter. Market reaction was not nearly as severe though as the sharp sell-off at the time of Nenegate in December 2015,

At the SA Reserve Bank's Monetary Policy Committee (MPC) meeting on 29-30 March, the MPC left the repo rate unchanged at 7.0%, citing an improved inflation outlook and subdued energy prices. February CPI slowed to 6.3% y/y from 6.6% y/y in January as food prices fell; however, this welcome development was quickly overtaken by the subsequent Cabinet reshuffle and downgrades. GDP growth for Q4 2016 slumped to -0.3% q/q annualised, from an upwardly revised 0.4% q/q annualised in Q3, as mining and manufacturing output shrank. For 2016 as a whole, the economy grew by 0.3% versus 1.5% in 2015, and growth is expected at 1.1% in 2017.

In SA listed property, we marginally increased our overweight exposure in our multi-asset funds in January. Yields are currently at slightly attractive levels following the market's negative reaction to the cabinet reshuffle. At quarter-end, listed property companies (excluding developers) were priced to return approximately 16% p.a. over the medium-term (assuming no change in the market's valuation of property), comfortably above inflation and, we believe, ample compensation for the risk involved.

Actual delivered growth in distributions per share for the major listed property companies averaged 9.1% for the quarter.

We estimate that one-year forward earnings forecasts for the SAPY, excluding developers, grew by just over 9.3% on an annualized basis over the quarter. This implies slight upgrades to forecasts for the sector (relative to expectations), given that consensus forecasts have previously been for growth rates of around 8.1%.

Within the major listed property sectors, office fundamentals remain fragile as a result of the weak SA economic environment and the sector's macro drivers. In retail, trading densities (measured by turnover/retail space) have fallen to levels below inflation for the first quarter of the year. Results from retail-focused Hyprop confirm this downward pressure on trading density growth, with cannibalization of sales from new and competing centres being a factor contributing to this phenomenon.

STRATEGY AND OUTLOOK

With the return of liquidity to the listed property market in January, Prudential completed a slight up-weighting of property allocations in our multi-asset funds which was first initiated in late December. The completion of this trade took our multi-asset funds to 2% overweight property, a position that was held through the remainder of the quarter.

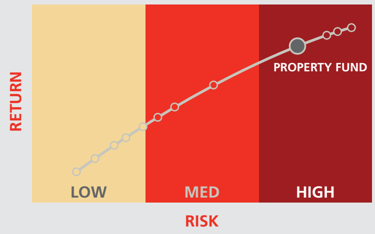
Relative to inflation-linked bonds (ILBs), we view the current valuations as slightly-attractive-to-fairly-valued. In the absence of a material de-rating in the market's valuation, listed property is priced to comfortably deliver double-digit returns over the medium term, well above inflation.

An important aspect of the investment case for listed property is illustrated by comparing property yields to those from ILBs. At quarter-end the SAPY, excluding developers, was priced to deliver a one-year forward distribution yield of 7.6%. This yield exceeded 10-year ILB yields by more than 5%. Assuming yields remain constant, property should outperform ILBs by at least 5%. In our view, this return premium is commensurate with the elevated risks of investing in listed property at present. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	D CLASS
1 year	2.3%	1.5%	2.4%	2.5%
3 years	15.4%	14.5%	n/a	15.5%
5 years	16.3%	15.8%	n/a	16.4%
7 years	16.6%	16.4%	n/a	n/a
10 years	14.4%	14.2%	n/a	n/a
Since inception	16.6%	16.6%	4.7%	17.2%

Inception date D Class: 1 July 2010, T Class: 1 April 2015

RISK/RETURN PROFILE:



FUND MANAGERS:
Duncan Schwulst

ASISA CATEGORY:
South African - Real Estate - General

BENCHMARK:
FTSE/JSE South African Listed Property Index (J253)

INCEPTION DATE:
2 December 2005

FUND SIZE:
R6 827 921 930

AWARDS:
Morningstar/Standard & Poor's: 2011

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL DIVIDEND MAXIMISER FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

PERFORMANCE

The fund produced a return of 2.7% for the three months ended March 2017, outperforming the average of the General Equity funds by 0.3% for the same period. On a rolling 12-month basis, the Prudential Dividend Maximiser Fund has outperformed the average of the General Equity funds by close to 2%.

MARKET OVERVIEW

The first quarter of 2017 saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China experienced one of its strongest starts to a year in equities, helped by low market volatility and improving economic and corporate fundamentals. In South Africa, local investment conditions appeared to be improving, however much of this progress was erased by the South African Cabinet reshuffle in the last week of March and the consequent downgrades of the country's sovereign credit rating to non-investment grade status by S&P Global and Fitch in April.

We acknowledge that while it is very difficult to forecast the future and we do not make any attempt to do this, we do spend a lot of time thinking about the economic cycles that various sectors are in, and where valuations are. In this way, we aim to try make money for our clients through these cycles and continue to try buy companies that have proven dividend and cash flow track records and which can withstand the normal upheavals that occur in markets over time. We therefore see this most recent setback as 'business as usual' and aim to continue building risk-cognisant portfolios that seek to add value through stock selection relative to benchmark.

STRATEGY AND POSITIONING

Our thinking therefore has been that, given the known potential for a credit rating downgrade, the fund's weighting to interest rate-sensitive stocks should be carefully monitored to ensure that we are not significantly overweight interest rate-sensitive stocks which would likely be most affected by a debt downgrade. The fund has therefore been underweight the retail and property sectors where the consumer continues to be under pressure and where valuations appear fairly full. We have, however, taken an active position in the banking sector, funded out of the underweight to retailers and property.

Those stocks that performed well during the 'reshuffle and downgrade' period included stocks that have foreign currency exposures such as Sappi, Glencore, Sasol, BHP Billiton, Naspers and British American Tobacco. Given the strength of the rand over the last year and the attractive valuation of some commodity shares and BAT, we had increased our weightings to these shares and the fund has therefore benefited and outperformed during the quarter.

The strongest contributor to performance over the quarter was the fund's investment in British American Tobacco, in which we have been long-standing shareholders. BAT has substantially lower capital expenditure requirements versus the average company and it is therefore able to deploy this strong cash flow to pay dividends, buy back shares and make strategic acquisitions. Many people assume that as cigarette volumes are flat or declining, the dividend growth from BAT must also be flat or declining. This could not be further from the truth, as BAT has managed to grow its dividends at a faster pace than most other large global staples companies. BAT is able to generate substantial cash flows and is able to more than offset cigarette volume declines with price increases.

We would like to remind our investors that when investing in the JSE, that they are not only buying South African exposure, but also shares in globally competitive and exposed businesses such as BHP Billiton, Naspers and BAT. In the case of the Prudential Dividend Maximiser Fund, we have in addition viewed foreign stocks as being relatively more attractive and currently over 25% of the fund is directly invested offshore across various markets. The fund's effective exposure to offshore cash flow and dividends is therefore well over 50%.

A smaller but notable contributor to performance in the first quarter was the fund's investment in Trencor, which saw its share price rally by just under 40% over the quarter. Trencor is essentially a holding company that owns 48% of US-listed Textainer, the world's second largest lessor of shipping containers. Textainer's profits have been under pressure for some time as a result of subdued global trade volumes and depressed steel prices. During the last quarter of 2016 we increased our position in Trencor when one of the worlds' biggest shipping lines, Korean shipping giant Hanjin, announced its bankruptcy. Textainer had rented 5% of its container fleet to Hanjin, which added to the negative sentiment towards the share. We viewed Textainer as hugely undervalued, but we thought Trencor was an even better bet as Trencor also has a large US dollar cash holding that represented almost 40% of its market cap at the time. The US dollar cash provided excellent downside risk protection, while the undervalued Textainer provided substantial upside potential. These are the types of investments we think are particularly valuable and which we spend a lot of time trying to identify for the fund.

The largest detractor from performance for the quarter was our investment in Barclays Group Africa. Within the banking sector, we view Barclays as being substantially undervalued, especially given that the market is already discounting the Barclays PLC overhang (caused by the intended selling down of their stake). It is attractive relative to other banks as it trades at a substantial discount despite similar growth prospects, dividend growth in real terms, and a dividend yield that exceeds its earnings yield multiple. We remain comfortable with this position and have used some of the negative price action following the credit rating downgrades to increase our overweight position in Barclays.

STRATEGY AND POSITIONING

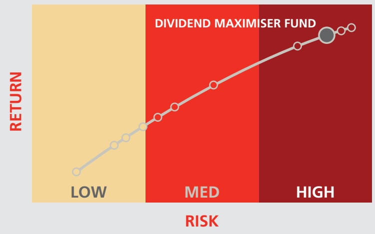
On market valuations, we currently view the market in South Africa as being fair value and caution that one should certainly expect a more moderate growth in dividends relative to the last five years, where dividends were recovering post the financial crisis. Earnings growth has been slowing and this may cause dividend growth to slow in the medium term. However, we still consider some offshore equity markets to be relatively undervalued and attractive, and therefore maintain the fund's offshore exposure.

The focus of the fund continues to be on finding companies that are undervalued and which are paying good dividend yields with the potential to pay growing dividends over the long run. We are confident that we have built a portfolio of attractively priced stocks that in aggregate is cheaper than owning the index, yet still capable of delivering attractive underlying growth independent of the economic cycle in which we find ourselves. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	B CLASS
1 year	3.0%	1.2%	3.2%	3.4%
3 years	5.7%	4.2%	n/a	6.2%
5 years	12.3%	9.9%	n/a	12.8%
7 years	12.1%	10.4%	n/a	12.6%
10 years	10.8%	8.1%	n/a	11.2%
Since inception	17.7%	14.4%	3.0%	11.8%

Inception date B Class: 2 January 2007, T Class: 2 January 2015

RISK/RETURN PROFILE:



FUND MANAGERS:

Ross Biggs, Craig Butters and Rehana Khan

ASISA CATEGORY:

South African - Equity - General

BENCHMARK:

ASISA South African – Equity - General Category Mean

INCEPTION DATE:

2 August 1999

FUND SIZE:

R4 558 986 970

AWARDS:

Raging Bull: 2006, 2008
Morningstar/Standard & Poor's: 2007, 2009

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL EQUITY FUND
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

PERFORMANCE

The Fund delivered another period of returns ahead of benchmark in the first quarter of 2017, such that on a rolling 12-month basis, the Prudential Equity fund has outperformed the benchmark by close to 5%. It is pleasing to note that after a disappointing period of underperformance in Q1 2016, our patience and conviction has been rewarded over the subsequent 12 months.

MARKET OVERVIEW

We would not want to discuss the first quarter without first addressing the dramatic events that unfolded on its final day, Zuma's cabinet reshuffle including the removal of well-respected Finance Minister Pravin Gordhan. This event led to South Africa's sovereign debt being downgraded to sub-investment grade by both S&P and Fitch the following week.

The market reaction was not dissimilar to what we witnessed at the time of Nene-gate in December 2015, albeit the price moves were more muted, as some would argue that Gordhan's departure did not come as a complete surprise. The rand immediately weakened by more than 10% and SA bond yields sold off 70bp to trade briefly above 9%. As a consequence, banking shares along with other interest-rate-sensitive shares such as general retailers and listed property fell sharply, while weak rand beneficiaries such as Naspers, British American Tobacco, Sappi and Sasol rallied.

While it is still early days and difficult to assess the lasting impact of these events, we are pleased to report that the portfolio has to date weathered the event better than was the case post Nene-gate. Going into the event we were cognisant of the increased risk of a sovereign downgrade and as a result were not as overweight banking shares as was the case at the end of 2015. In addition, we have been increasingly concerned about the general state of SA consumers and earnings prospects for the retail sector, such that the portfolio remains underweight the sector. This relative positioning partly cushioned the fund from the impacts of the event despite the bank share losses, with Barclays Africa being a notable detractor.

Within the banking sector, our largest overweight exposure is to Barclays Africa on the basis that its valuation is attractive relative to its own history while also trading at a discount to the other banks on both a PE and DY basis. The market remains concerned with not only the overhang associated with parent Barclays PLC's decision to sell down its stake, but also the uncertainty around the potential acquirer of these shares. However, with Barclays' consensus earnings growth prospects similar to the other banks and a dividend yield that exceeds its forward PE, we believe that these market 'worries' are already discounted in the price.

The fund did benefit from its exposure to a basket of industrial stocks that are beneficiaries of the weaker rand, such as British American Tobacco, Naspers and Richemont. In addition, the fund's positions in resource shares such as Anglo American, Exxaro, Sappi and Sasol helped mitigate against our limited exposure to the gold and platinum producers, which are more leveraged to the weakening rand.

Contributors

A key overweight position in British American Tobacco, and a mild overweight to Naspers were among the largest positive contributors to performance over the quarter, with both shares benefitting from the weakening rand in the final week of the quarter.

Aside from the weaker rand pushing the Naspers share price higher, the primary driver of its gains was the strong share performance of its holding in Tencent, which delivered a strong set of Q4 2016 results. The market re-rated the stock on a favourable outlook for its new foray into mobile payments and continued growth in mobile advertising.

Another notable contributor in Q1 was Trencor, which saw its share price rally by just under 40% over the quarter. We were presented with an opportunity to buy a significant block of Trencor shares in October last year. Trencor is a holding company that owns 48% of US listed Textainer, the world's second largest lessor of shipping containers. Textainer's lease rates and associated profits have been under pressure for some time as a result of subdued global trade volumes, a depressed steel price and the prevailing low interest rates. In addition, the announced liquidation of the Korean shipping giant Hanjin and disclosure from Textainer that approximately 5% of its container fleet was on contract to Hanjin, added to the negative sentiment towards the share. The market's primary concern was that Textainer would need to impair its container fleet carrying value due to a mark-to-market of the prevailing steel prices. At the time we purchased the Trencor block of shares, Textainer was trading at a 65% discount to its book value, but what made the trade even more compelling was the fact that Trencor also has a large US dollar cash holding that represented almost 40% of its market cap. This additional cash buffer, as well as the fact that both global steel prices and US interest rates had already started to rise, gave us comfort to buy a large stake in what we consider to be a quality business with dominant market share.

The additional purchases in Trencor were in part funded by the sale of our holding in Barloworld. Barloworld has enjoyed a significant re-rating and we believe it is now trading above its fair value.

PPC was another interesting contributor during the quarter, with the share price rising close to 17%. PPC is, along with Sasol and Sun International (discussed below), an example of a company where the market is attaching little value to "sunk capital", i.e., large capital spending projects that will bring them new future income streams. We continue to see significant future value in PPC's African cement projects which are nearing completion and have yet to contribute to the group's profits. During the quarter PPC announced that it has entered formal discussions with AfriSam to pursue a merger of the two businesses. While a merger should present an opportunity to remove duplicate costs and optimise production and logistics, we have some concerns about possible regulatory conditions that may be imposed, and the impact of an Afrisam acquisition on PPC's recently restored balance sheet.

Sasol continues on this theme, with investors attributing little value to the large investment the group is making in its Lake Charles US ethane cracker project, which is due to come on stream in the second half of 2018. Sasol had spent a cumulative US$6 billion on this as at the end of 2016. It appears that the share's current market valuation can be attributed largely to the spot rand oil price, with very little future contributions from this project being included in valuations – this is despite the company being closer to the end of its current capex cycle than the beginning, and the potential for cash flows from the new project in the next few years.

Detractors

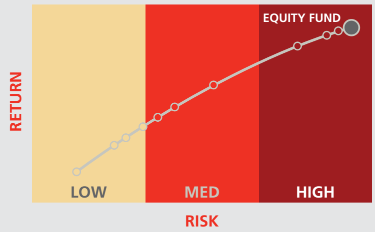
Notable detractors from the fund's performance over the quarter included the banks such as Barclays (discussed above) and Firstrand, following the cabinet reshuffle that resulted in the sovereign rating downgrade. The consequent downgrades of the South African banks' own credit ratings will result in higher offshore borrowing costs for them, although currently only a small percentage of their debt comes from foreign sources.

Apart from the banks, our preferred hospital stock, Netcare, fell nearly 15% on a disappointing trading update in which management cited reduced patient volumes. It appears that medical funders, such as Discovery, have tightened up on hospital admission authorisations which has impacted on patient day volumes for both Netcare and Life Healthcare. While we anticipate that this trend will continue to impact utilisation in the coming financial year, we continue to hold a position in Netcare given that its valuation multiple is now trading at an approximate 25% discount to both Mediclinic and Life Healthcare.

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	6.1%	1.2%	6.5%
3 years	6.3%	4.2%	6.7%
5 years	13.0%	9.9%	13.5%
7 years	12.9%	10.4%	13.5%
10 years	11.0%	8.1%	11.6%
Since inception	17.7%	14.4%	12.5%

Inception date B Class: 2 January 2007

RISK/RETURN PROFILE:



FUND MANAGERS:
Chris Wood and Johny Lambridis

ASISA CATEGORY:
South African - Equity - General

BENCHMARK:
ASISA South African - Equity - General Category Mean

INCEPTION DATE:
2 August 1999

FUND SIZE:
R2 603 800 712

AWARDS:
Raging Bull: 2006, 2007, 2008
Morningstar/Standard & Poor's: 2007, 2008

Sources: Prudential, Morningstar & Deutsche Securities

Sun International also had a poor quarter following its disappointing earnings update which revealed a lack of top-line earnings growth and margin pressure. Our investment case in Sun International is not premised on a return to growth in their existing casinos, but instead we project revenue growth to come from the newly built Menlyn Maine casino in Pretoria, their Latin American ventures, and recently acquired GP Slots business. The large upfront costs associated with constructing the new Menlyn casino have seen an increase in debt, but with no profit contribution yet in the base as a result of the casino only opening in April 2017. We believe Sun International is poised to return to growth this year and will experience a significant reduction in capex following the completion of Menlyn, which will enable the group to begin reducing debt on its balance sheet. Sun International now trades on an undemanding forward earnings multiple of less than 10x that we find offers compelling value relative to other SA consumer cyclical businesses.

International Assets

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. International equity was a solid contributor as equity markets rallied, overshadowing the general rand appreciation over the quarter.

PORTFOLIO CHANGES

Notable changes to the portfolio in the quarter included reducing BHP Billiton in favour of the inclusion of Exxaro. We find the implied value of Exxaro's SA coal assets to be very attractively priced when one deducts the value of its investment in US-listed Tronox, and value its stake in Sishen Iron Ore Company using Kumba as a proxy. Exxaro have announced they intend to sell their Tronox stake and are in the process of finalising a new BEE deal. We are confident that the simplification of Exxaro's structure will lead to a re-rating of the underlying coal business, which has a strong underpin to its future earnings given that Eskom's newly built Medupi coal-fired station will be dependent on coal supplied from Exxaro's Grootgeluk mine.

OUTLOOK

It remains difficult to predict what may arise as a result of the unexpected cabinet reshuffle and subsequent rating downgrades, and there remains a great deal of uncertainty about future political policy, and how this will impact on investor sentiment and the currency. Instead of attempting to forecast the unknowns, we focus our efforts on valuations of companies and identifying where they are in their respective earnings cycles. We aim to produce strong returns for our clients through these cycles and continue to invest in companies that have proven earnings track records and can withstand the continually changing risks in financial markets over time.

We are confident that we have built a portfolio of attractively priced stocks that in aggregate is cheaper than owning the index, yet still capable of delivering attractive underlying growth independent of the economic cycle in which we find ourselves. ■

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL HIGH YIELD BOND FUND OF FUNDS
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL INCOME

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. By contrast, South Africa suffered setbacks with the Cabinet reshuffle and ensuing downgrade of its sovereign credit rating to non-investment grade status by two ratings agencies in late March and early April. This saw the rand depreciate about 8% against the US dollar during the last trading week of March; however, the local currency still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro.

In the US, as in the previous quarter, stronger-than-expected GDP growth (at 2.1% in Q4 2016 q/q annualised) combined with a tighter jobs market, as well as firming inflation, to reinforce the widely expected Fed rate hike of 25bps in March. FOMC members' consensus forecasts indicated a further two 25bp rate hikes in 2017 given the underlying healthy economy. In turn, the interest rate market was also discounting at least another two 25bp increases this year.

The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, managed to return 1.8% in the quarter, reversing some of Q4 2016's sharp losses as 10-year yields of over 2% attracted investors. US investment grade corporate bond spreads versus USTs narrowed only marginally to 122bps from 129bps, while high-yield bond spreads fell by around 37bps (led by telecom and healthcare companies rather than the energy sector this quarter). A slightly weaker US dollar vs the yen and euro also lifted bond returns from these markets.

In the Eurozone, worries of a populist victory in the Netherlands' election were put to rest as the far-right party lost by a sound margin. French elections will be the next test: the anti-euro nationalist party is expected to perform well. The region's Q4 2016 GDP growth was reported steady at 1.8% (q/q annualised), fuelled by the ECB's ongoing easy monetary policy, while inflation picked up to 2% y/y in February, mostly on the back of higher energy costs. Although Britain served its formal "Brexit" notice to the EU in March and its ability to negotiate favourable exit terms appeared increasingly difficult, UK economic data was upbeat. Sterling remained weak, however, spurring more inflation worries for 2017, while the Bank of England refrained from raising interest rates.

In Japan, Q4 2016 GDP growth disappointed slightly at 1.0% q/q annualised from a revised 1.4% in the previous quarter - private consumption was essentially flat while export growth accelerated. The Finance Minister said the economy remained in a "moderate recovery" after four quarters of expansion, with the job market improving. Core inflation (excluding fresh food prices) also rose to 0.2% y/y in February due to higher energy prices.

In China, 2017 started strongly amid improving corporate fundamentals, solid investor demand and low volatility. The yuan's exchange rate stabilised on the back of the improving global trade outlook, and concerns over growth and previous market volatility receded. GDP growth for Q4 2016 was reported at 6.8% (q/q annualised), slightly above the 6.7% expected, as consumer spending accelerated and the property market rebounded. Other emerging market assets, including both bonds and equities, recorded good gains amid renewed investor demand for risk assets.

In commodities, the oil price softened somewhat to trade around US$50/barrel at quarter-end from around $55 at the start of the year as the effects of a curtailed supply stemming from the OPEC agreement were offset to some extent by rising supplies from the US. Brent crude fell 7.0% over the quarter. Most other commodity prices were firmer, however, on signs of improving global growth and re-emerging inflationary pressures. Gold gained 8.9% in Q1, while platinum rose 5.2% and palladium was up 19.1%. Other good gains were recorded by aluminium (+14.6%), lead (+16.6%) and zinc (+7.5%).

PERFORMANCE

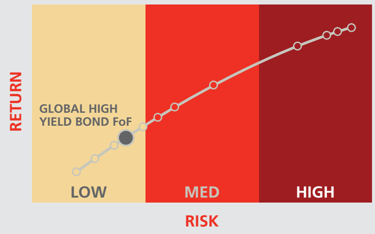
For the quarter ending 31 March 2017, the fund returned -0.2% (net of fees, in rand), outperforming the -2.6% returned by its benchmark, the Barclays Capital Global Aggregate Bond Index (in rand). While global bonds largely posted positive returns over the quarter in US$ terms, these were offset by the modest rand appreciation over the period. In absolute performance terms, the fund's returns were dented by weakness in US and European investment-grade corporate bonds over the period, but these were offset to a large extent by the fund's Japanese yen cash holdings. The outperformance versus the benchmark was a function of the fund's higher exposure to corporate bonds, which performed better over the quarter than their sovereign counterparts. For the past 12 months, the fund has returned -7.8% p.a. (net of fees), outperforming its benchmark which returned -12.5% while over the past five years the fund has returned a net 12.8% p.a., above its benchmark of 11.7%.

STRATEGY AND OUTLOOK

We remain concerned about prospective returns from global sovereign bonds given the low yields on offer and potential for rising interest rates, and therefore continue to be underweight sovereign bonds and underweight duration. We also continue to hold cash (at approximately 25% of the fund's weight at quarter-end), floating rate notes and shorter-term bonds in order to reduce this interest rate risk. We remain overweight investment-grade corporate bonds that offer more attractive relative yields and valuations. During the quarter we sold much of our exposure to high-yield corporate bonds: with the fund having benefitted significantly from our allocation to these assets following their strong performance, we took profits and now have very little high yield exposure. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	-7.8%	-12.5%
3 years	6.7%	7.2%
5 years	12.8%	11.8%
7 years	11.7%	10.9%
10 years	10.4%	9.6%
Since inception	8.8%	8.7%

RISK/RETURN PROFILE:



FUND MANAGERS:
David Knee and Michael Moyle

ASISA CATEGORY:
Global - Interest Bearing - Variable Term

BENCHMARK:
Barclays Capital Global Aggregate Bond Index

INCEPTION DATE:
1 November 2000

FUND SIZE:
R240 727 543

AWARDS:
Raging Bull: 2006, 2008, 2013
Morningstar/Standard & Poor's: 2007, 2009, 2013

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL CAUTIOUS MANAGED FUND OF FUNDS
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL MULTI-ASSET

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China experienced one of its strongest starts to a year in equities, helped by low market volatility and improving economic and corporate fundamentals. By contrast, South Africa suffered setbacks with the Cabinet reshuffle and ensuing downgrade of its sovereign credit rating to non-investment grade status by two ratings agencies in late March and early April. This saw the rand depreciate about 8% against the US dollar during the last trading week of March; however, the local currency still managed to appreciate over the three-month period by 2.2% against the US dollar, by 1.2% against the pound sterling and by 0.8% versus the euro.

In the US, as in the previous quarter, stronger-than-expected GDP growth combined with a tighter jobs market, as well as firming inflation, to reinforce the widely expected Fed rate hike of 25bps in March. FOMC members' consensus forecasts indicated a further two 25bp rate hikes in 2017 given the underlying healthy economy.

The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, managed to return 1.8% in the quarter, reversing some of Q4's sharp losses as 10-year yields of over 2% attracted investors. In the equity market, stocks rallied strongly, boosted by hopes of higher government spending, corporate tax cuts and deregulation under Trump: the S&P 500 returned 6.1% and the Nasdaq 12.1% for the quarter. In the Eurozone and UK, similar conditions saw the Dow Jones Eurostoxx 50 return 8.3%, while Germany's DAX returned 8.8%, the French CAC 7.1% and the FTSE 100 5.3% (all in US$). Finally, the Nikkei 225 Index returned 4.5% (in US$).

The MSCI China posted a total return of 12.9% (in US$) in Q1 – its best start in years – amid improving corporate fundamentals, solid investor demand and low volatility. GDP growth for Q4 2016 was reported at 6.8% (q/q annualised), slightly above the 6.7% expected, as consumer spending accelerated and the property market rebounded. Other emerging market assets, including both bonds and equities, recorded good gains amid renewed investor demand for risk assets. Overall, the MSCI Emerging Markets Index returned an impressive 11.4% in US$, compared to 6.4% from the MSCI World Free Index for developed markets.

PERFORMANCE

For the quarter ending 31 March 2017, the fund returned 0.9% (net of fees in rand), ahead of the 0.0% from its benchmark (the average return of the ASISA Global Multi-Asset Low Equity sector). In absolute terms, positive global equity returns, assisted by favourable stock selection and overweight allocations to European equities and also the Indian market, were partially offset by negative returns from global bonds and cash.

STRATEGY AND OUTLOOK

In global fixed income, we remain concerned about prospective returns from global sovereign bonds given the low yields on offer and potential for rising interest rates, and therefore continue to be underweight sovereign bonds and underweight duration. We also continue to hold cash and shorter-term bonds in order to reduce this interest rate risk. We remain overweight investment-grade corporate bonds, with smaller overweights to listed property and cash. During the quarter we sold much of our exposure to high-yield corporate bonds: with the fund having benefitted significantly from our allocation to these assets following their strong performance, we took profits and now have very little high yield exposure.

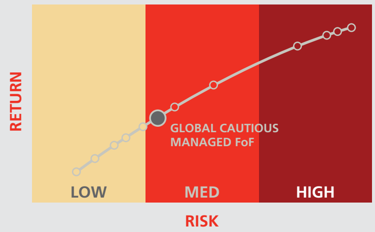
For global equities, the ongoing rally in many global equity markets (especially the US) has kept valuations at relatively high levels on the basis of both 12-month forward P/E and price-to book measures. However, because equities are less expensive than government bonds, we prefer the former to the latter in the fund, with a 40% weighting. Over the quarter equity risk premiums (the yield on equities versus bonds) narrowed, but still provide a substantial valuation buffer that should help to protect equities in the event of growth disappointment.

The portfolio has maintained an 8.9% weighting to global listed property, where yields are mid-single digit and consequently higher than what is achievable from global government bonds (where, as noted, the fund is underweight).

Looking ahead, the brighter outlook for global growth and trade should help broadly to underpin global equity markets while risk for government bonds remains elevated as countries gradually unwind their supportive monetary policies. Meanwhile, South Africa's new sub-investment grade credit rating status and uncertainty around our fiscal policy implementation, governance standards and political risk will keep financial market volatility elevated in the months ahead. Importantly, the extent of further rand depreciation following the downgrades will impact on global asset values for rand-based investors. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	-4.7%	-5.6%
3 years	8.4%	8.7%
5 years	12.8%	12.8%
7 years	10.2%	10.2%
10 years	6.3%	6.3%
Since inception	7.7%	7.2%

RISK/RETURN PROFILE:



FUND MANAGERS:
Michael Moyle, David Knee and Marc Beckenstrater

ASISA CATEGORY:
Global - Multi-Asset - Low Equity

BENCHMARK:
ASISA Global - Multi-Asset - Low Equity Category Mean

INCEPTION DATE:
1 March 2004

FUND SIZE:
R91 275 709

HOW TO INVEST

0860 105 775

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query@myprudential.co.za

Application forms

Invest now

Application forms and all required documentation must be faxed to **+27 11 263 6143** or e-mailed to **instructionsa@myprudential.co.za.**

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL VALUE FUND OF FUNDS
31 MARCH 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL EQUITY

MARKET OVERVIEW

The first quarter of 2017 (Q1) saw a very positive start to the year as global financial markets were underpinned by generally improving macroeconomic data and bullish investor sentiment that drove good demand for both developed and emerging market assets. In the US, the "Trump reflation" trend continued, pushing equity markets still higher, while surprisingly robust growth in the UK and steady growth in Europe bolstered markets there. China experienced one of its strongest starts to a year in equities, helped by low market volatility and improving economic and corporate fundamentals.

PERFORMANCE

The Fund was flat against its benchmark, the MSCI All Countries World Index, returning 4.5% in rand terms over the quarter.

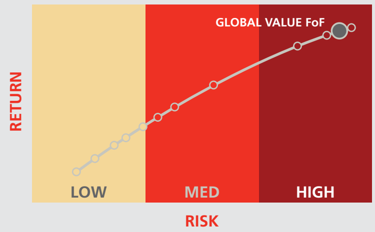
Stock selection in Japan and the UK, as well as our tactical overweight to India, added to performance during the quarter. The fund's underweight position in China detracted from performance as Asia recorded the strongest regional performance of the benchmark for the quarter.

STRATEGY AND OUTLOOK

As in previous quarters, our overweight exposures remain concentrated in European markets where long-standing growth concerns have kept valuations on the cheap side of fair value, as well as selected emerging markets including India, funded by underweights in the US, Japan and a variety of other smaller markets including Australia, where valuations are more expensive. Over the quarter equity risk premiums (the yield on equities vs bonds) narrowed, but still provide a substantial valuation buffer that should help to protect equities in the event of growth disappointment. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	5.7%	2.6%
3 years	12.6%	13.1%
5 years	19.6%	20.7%
7 years	15.0%	17.3%
10 years	7.9%	10.3%
Since inception	6.8%	7.9%

RISK/RETURN PROFILE:



FUND MANAGERS:
Michael Moyle and Marc Beckenstrater

ASISA CATEGORY:
Global - Equity - General

BENCHMARK:
MSCI All Country World Index (Net)

INCEPTION DATE:
18 February 2000

FUND SIZE:
R225 712 046

HOW TO INVEST

0860 105 775

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Application forms

Invest now

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Sources: Prudential, Morningstar & Deutsche Securities