PRUDENTIAL UNIT TRUSTS QUARTERLY COMMENTARY
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

COMBINED QUARTERLY COMMENTARY

INCOME | MULTI-ASSET | PROPERTY/EQUITY | GLOBAL

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PRUDENTIAL MONEY MARKET FUND
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

INCOME FUND

PERFORMANCE

Over the past quarter, the fund delivered a return of 1.8% (net of fees) versus its benchmark the STeFI Call Deposit Index which returned 1.7%. The average duration of the fund at quarter end was 53 days relative to the 90 day maximum average duration.

MARKET OVERVIEW

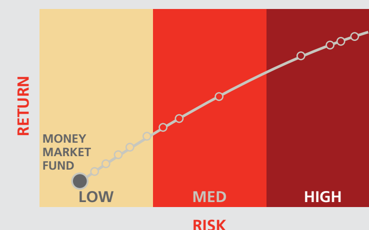
The quarter's political and credit ratings news managed to overshadow some of the fundamentals: SA's Q3 GDP growth was reported at 2.0% (q/q, annualised), with agriculture, mining and manufacturing the main drivers of the expansion. In the first nine months of 2017, the South African economy grew by 1.0% y/y. At the same time, November CPI eased to 4.6% y/y from 4.8% in October, helping underpin interest-rate-sensitive assets like bonds and listed property. Despite the improving inflation data, the SA Reserve Bank (SARB) opted to leave interest rates on hold over the quarter, citing upside risks to inflation from possible rand weakness, further downgrades and political uncertainty. However, the recent rand rally could mitigate the SARB's view, helping to ease inflationary pressures in 2018.

PPI inflation rose marginally to 5.1% y/y in November from 5.0% y/y in October, mainly attributable to coke, petroleum, chemical, rubber and plastic products. Month-on-month, PPI came in at 0.5%. Private sector credit extension (PSCE) rose to 6.5% y/y for November from 5.4% y/y in October. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	X CLASS
1 year	7.6%	6.9%	7.7%
3 years	7.0%	6.5%	7.1%
5 years	6.3%	5.9%	6.5%
7 years	6.0%	5.7%	n/a
10 years	7.0%	6.7%	n/a
Since inception	7.8%	7.6%	6.2%

Inception date X Class: 1 April 2011

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:
R1 545 135 965

DISCLAIMER

Prudential Portfolio Managers Unit Trusts Ltd (Registration number: 1999/0524/06) is an approved CISCA management company (#29). Assets are managed by Prudential Investment Managers (South Africa) (Pty) Ltd, which is an approved discretionary Financial Services Provider (#45199). The Trustee's/Custodian details are: Standard Bank of South Africa Limited - Trustee Services & Investor Services. 20th Floor, Main Tower, Standard Bank Centre, Heerengracht, Cape Town. Collective Investment Schemes (unit trusts) are generally medium-to long-term investments. Past performance is not necessarily a guide to future investment performance. Unit trusts are traded at the ruling forward price of the day, meaning that transactions are processed during the day before you or the Manager know what the price at the end of the day will be. The price and therefore the number of units involved in the transaction are only known on the following day. The unit trust fund may borrow up to 10% of the fund value, and it may also lend any scrip (proof of ownership of an investment instrument) that it holds to earn additional income. A Prudential unit trust fund may consist of different fund classes that are subject to different fees and charges. Where applicable, the Manager will pay your financial adviser an agreed standard ongoing adviser fee, which is included in the overall costs of the fund. A Collective Investment Schemes (CIS) summary with all fees and maximum initial and ongoing adviser fees is available on our website. One can also obtain additional information on Prudential products on the Prudential website. The Manager may, at its discretion, close your chosen unit trust fund to new investors and to additional investments by existing investors to make sure that it is managed in accordance with its mandate. It may also stop your existing debit order investment. The Manager makes no guarantees as to the capital invested in the fund or the returns of the fund. Excessive withdrawals from the fund may place the fund under liquidity pressure and, in such circumstances; a process of ring fencing withdrawal instructions and managed pay outs over time may be followed. A money market fund is not a bank deposit account. The Prudential Money Market Fund aims to maintain a constant price of 100 cents per unit. A forward looking yield is used. This means that the last seven days' yield (less the maximum service charges, including VAT) is taken and is annualised for the next 12 month period, assuming the income returns are reinvested. Yields for money market funds are published daily. The purpose of the money market yield is to indicate to investors a compounded annual return for all money market portfolios on a comparable basis. The yield calculation is not used for income distribution purposes. The total return to the investor is primarily made up of interest received but may also include any gain or loss made as a result of a default by an issuer of any instrument held by the fund. This can have the effect of a capital loss. Such losses will be borne by the Prudential Money Market Fund and its investors and in order to maintain a constant price of 100 cents per unit, investors' unit holdings may be reduced to the extent of such losses. Fund prices are published daily on the Prudential website. These are also available upon request. The performance is calculated for the portfolio. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Purchase and repurchase requests must be received by the Manager by 11h30 for Money Market SA time each business day. All online purchase and repurchase transactions must be received by the Manager by 10h30 (for all Funds) SA time each business day.

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL HIGH INTEREST FUND
31 DECEMBER 2017

QUARTERLY COMMENTARY

INCOME FUND

PERFORMANCE

The Prudential High Interest Fund generated a return of 1.9% (net of fees) for the quarter compared to its benchmark, the STeFI Composite Index which returned 1.8%.

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 days weighted average maturity.

Relative to the 180 day maximum average duration, the quarter end duration of the fund came in at 40 days.

MARKET OVERVIEW

Despite the sluggish local economy, elevated political risk and further credit rating downgrades during the quarter, South African assets performed surprisingly strongly. Although bonds and listed property experienced sharp sell-offs after the revelation of SA's deteriorating fiscal position in October's Medium-Term Budget Policy Statement (MTBPS), they both managed a relief rally following Moody's postponement of its credit rating decision in late November, and saw even better gains in the "Ramaphosa rally" amid the post-ANC conference exuberance in December. Investors were keen to snap up the attractive yields on offer. The BEASSA All Bond Index returned 2.2% for the quarter and a strong 10.2% for the year. Inflation-linked bonds (Composite ILB Index) produced a more muted 1.0% for Q4 and 2.9% in 2017, while cash as measured by the STeFI Composite Index delivered 1.8% in the quarter and 7.5% for the year. Finally, SA listed property produced 8.3% in Q4, for an unexpectedly robust total return of 17.2% in 2017.

Equities, meanwhile, were helped by global enthusiasm over the quarter: the FTSE/JSE All Share Index hit new record highs in November, rising briefly to 61,299 points before retracing about 3% to close December at around 59,500 points. The market suffered a significant drop in early December on the back of the plunge in the share prices of Steinhoff and associated companies such as Steinhoff Africa Retail (STAR) and Brait. This was partially offset by the Ramaphosa rally, led by retail and banking stocks, but rand strength hit the share prices of those companies with significant offshore earnings, including industrial and resources counters.

For the quarter, the ALSI returned 7.4%, thanks to a 16.0% return from Financials and a 22% return from retailers, both boosted by the stronger rand and an improved local outlook. Resources returned 3.6% and Industrials as a sector delivered 4.7%, with Property returning 8.3%. For 2017 as a whole, the ALSI had a remarkable year given the poor local fundamentals, producing a total return of 21.0%, most of which came in the second half. Among the sectors, it was Industrials that returned the most with 22.5% (led by Naspers with a total return of 72%), while Financial stocks delivered 20.6%, listed Property 17.2% and Resources 16.8%. Excluding Naspers, the ALSI would have returned only around 13% for the year.

The quarter's political and credit ratings news managed to overshadow some of the fundamentals: SA's Q3 GDP growth was reported at 2.0% (q/q, annualised), with agriculture, mining and manufacturing the main drivers of the expansion. In the first nine months of 2017, the South African economy grew by 1.0% y/y. At the same time, November CPI eased to 4.6% y/y from 4.8% in October, helping underpin interest-rate-sensitive assets like bonds and listed property. Despite the improving inflation data, the SA Reserve Bank (SARB) opted to leave interest rates on hold over the quarter, citing upside risks to inflation from possible rand weakness, further downgrades and political uncertainty. However, the recent rand rally could mitigate the SARB's view, helping to ease inflationary pressures in 2018.

Finally, the rand also benefited from the December Ramaphosa rally, as well as the positively perceived Moody's reprieve. Despite Q4's high volatility, the local currency managed to appreciate 8.8% against the US dollar and 7.5% against the euro over the period. For the entire year it gained 10.1% versus the greenback and 1.9% versus UK sterling, but depreciated 2.2% against the robust euro.

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.

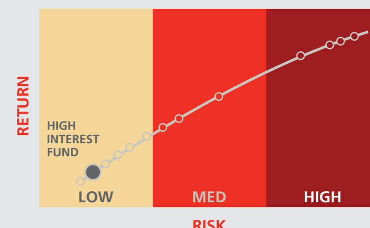
Exposure to floaters in the 3-year space was maintained over the quarter on the back of attractive pricing. While credit issuance has been scarce since 2016, mixed with a tightening of credit spreads, the quarter did see a number of banks and corporates coming to market, after some hesitance following the downgrade of the sovereign credit rating. Issuances were generally well supported and largely cleared towards the mid-point or lower end or through guidance.

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	8.3%	7.6%	8.4%	8.5%
3 years	7.6%	7.1%	7.7%	7.8%
5 years	6.8%	6.5%	6.9%	7.1%
7 years	6.5%	6.2%	n/a	6.8%
Since inception	6.5%	6.2%	6.6%	6.8%

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

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:
R11 420 347 450

PLEASE NOTE:
This fund is capped to new investors

DISCLAIMER
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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL HIGH YIELD BOND FUND
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

INCOME FUND

PERFORMANCE

For the quarter, the fund returned 2.2% (net of fees) closely matching 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 1.0% (JSE CILI). We began the quarter with a neutral duration position and added duration when bonds experienced a sharp sell-off post the Medium-Term Budget Policy Statement (MTBPS) in October. Towards the end of the quarter bonds rallied following Moody's postponement of its credit rating decision and the ANC conference which saw us closing our position and ending the quarter once again with a neutral duration. 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.

MARKET OVERVIEW

In the US, the latest GDP data (Q3) showed growth accelerating to 3.3% (q/q annualised) from 3.1%, propelled by higher business investment and rising inventories, while consumer confidence reached a 17-year high in November. Meanwhile, consumer inflation remained at moderate levels: November CPI came in at 2.2% y/y, in line with expectations, with the small rise from October's 2.0% y/y attributable mainly to rising oil prices. Taking this expansion together with full employment and the large corporate tax cuts passed by the US legislature in December, analysts expect inflation to become more problematic in 2018 – market consensus suggests four 25bp Fed rate hikes in the new year following its 25bp increase in December.

In the Eurozone, the region grew a stronger-than-expected 2.5% (q/q annualised) in Q3, up from a revised 2.3% in Q2, as the recovery became more broad-based across many euro-area countries, and helped by the ECB's ongoing easy monetary policy. Economic growth is now forecast at 2.2% y/y for 2017, the fastest in a decade. Despite the unemployment rate falling to a nearly nine-year low of 8.8%, inflation remained becalmed with CPI at 1.5% y/y in November. Meanwhile, the euro continued its appreciation in Q4, gaining 12.7% for the year as investors bet on accelerating Eurozone growth while the US business cycle aged. At its December meeting the ECB left interest rates on hold as expected, given subdued inflation.

The UK continued to face a Brexit-inspired dilemma, with uncertainty curtailing economic growth but fuelling inflation from the weaker pound. Although progress was finally made in Brexit negotiations during the quarter, Q3 GDP growth was only 1.5% (q/q annualised), while November CPI surprised to the upside at 3.1% y/y. The Bank of England opted to raise interest rates by 25bps in November, its first hike since 2007 - investors now expect no further hikes until late 2018.

In Japan, Q3 GDP growth came in at 1.4% (q/q annualised), down from a revised 2.6% in Q2, but still solid as expanding exports compensated for softer consumer demand. This marked seven successive quarters of growth. However, core inflation was still tepid at only 0.9% y/y in November. Prime Minister Abe comfortably won the snap election he called in October.

In China, Q3 GDP growth slowed marginally as expected, to 6.8% (q/q annualised) from 6.9% in Q2, dented by the government's attempts to rein in property market speculation and reduce debt. This is still above 2017's official 6.5% growth target, with factory output boosted by improving global trade.

In commodities, the price of Brent crude jumped some 16% during the quarter to end the year at over US$66.50 per barrel, up nearly 18% for 2017 as a whole as OPEC and other producers' successfully curbed supply in the latter half of the year and look set to extend production cuts through the end of 2018.

Despite the sluggish local economy, elevated political risk and further credit rating downgrades during the quarter, South African assets performed surprisingly strongly. Although bonds and listed property experienced sharp sell-offs after the revelation of SA's deteriorating fiscal position in October's MTBPS, they both managed a relief rally following Moody's postponement of its credit rating decision in late November, and saw even better gains in the "Ramaphosa rally" amid the post-ANC conference exuberance in December.

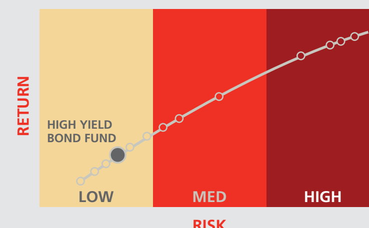
The quarter's political and credit ratings news managed to overshadow some of the fundamentals: SA's Q3 GDP growth was reported at 2.0% (q/q, annualised), with agriculture, mining and manufacturing the main drivers of the expansion. In the first nine months of 2017, the South African economy grew by 1.0% y/y. At the same time, November CPI eased to 4.6% y/y from 4.8% in October. Despite the improving inflation data, the SA Reserve Bank (SARB) opted to leave interest rates on hold over the quarter, citing upside risks to inflation from possible rand weakness, further downgrades and political uncertainty. However, the recent rand rally could mitigate the SARB's view, helping to ease inflationary pressures in 2018.

Finally, the rand also benefited from the December Ramaphosa rally, as well as the positively perceived Moody's reprieve. Despite Q4's high volatility, the local currency managed to appreciate 8.8% against the US dollar and 7.5% against the euro over the period. For the entire year it gained 10.1% versus the greenback and 1.9% versus UK sterling, but depreciated 2.2% against the robust euro. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	7.6%	8.2%	7.9%
3 years	7.0%	7.6%	7.3%
5 years	5.8%	6.3%	6.2%
7 years	7.4%	7.7%	7.7%
10 years	8.2%	8.4%	8.5%
Since inception	10.2%	10.5%	9.1%

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:
R540 190 396

DISCLAIMER
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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL ENHANCED INCOME FUND
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

PERFORMANCE

For the 12 months ended 31 December 2017 the fund delivered 8.2% (net of fees) outperforming its benchmark as measured by the STeFI Composite Index by 0.6%. For the quarter ending 31 December 2017 the fund returned 1.2% (net of fees), modestly underperforming its benchmark by 0.6%.

MARKET OVERVIEW

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole. The longstanding rally looked set to continue into the new year amid ongoing optimism over the health of the global economy, still-subdued inflation, supportive monetary policies and bullish investor sentiment, given an additional fillip by the enactment of major corporate tax cuts in the US. The US Federal Reserve continued its very gradual tightening, the Bank of England hiked interest rates for the first time in a decade, and the European Central Bank (ECB) kept interest rates unchanged. Global bonds posted a muted return amid mixed sentiment over prospects for rising inflation and interest rates.

For South African investors it was a surprisingly positive quarter, with all local asset classes managing to post solid returns, especially in the wake of the rally sparked by market-friendly Cyril Ramaphosa's election as the new President of the ANC in December. Despite the installation of a divided ANC leadership committee with competing policy approaches, investors interpreted Ramaphosa's election as an opportunity for the country to introduce much-needed reforms, reduce corruption, and lift business and consumer sentiment. Greater prospects for improved fiscal responsibility also helped the credit rating outlook. Combined with Moody's credit rating reprieve in November, this more optimistic sentiment helped lower risk perceptions among both local and offshore investors, driving strong rallies in South African bonds and the rand. SA equities, although returning a respectable 7.4% for the quarter, were adversely affected in December by the collapse in the share prices of Steinhoff and its associated companies, counterbalanced partly by a rise in domestically oriented shares (including banks and retailers) post the ANC elective conference.

In the US, the latest GDP data (Q3) showed growth accelerating to 3.3% (q/q annualised) from 3.1%, propelled by higher business investment and rising inventories, while consumer confidence reached a 17-year high in November. This marked the 32nd consecutive quarter of US economic expansion since the 2009 recession, the third longest since 1945. Meanwhile, consumer inflation remained at moderate levels: November CPI came in at 2.2% y/y, in line with expectations, with the small rise from October's 2.0% y/y attributable mainly to rising oil prices. Taking this expansion together with full employment and the large corporate tax cuts passed by the US legislature in December, analysts expect inflation to become more problematic in 2018 – market consensus is for four 25bp Fed rate hikes in the new year following its 25bp increase in December. However, new Fed Chairman Jerome Powell is expected to proceed gradually - in line with his predecessor, Janet Yellen, he is seen as having a dovish approach to managing monetary policy. Into 2018 the Fed will also continue to wind down its balance sheet, having started in October with an outstanding $4.5 trillion in US Treasury bonds and mortgage-backed securities that it will slowly allow to mature, without reinvesting the proceeds. Under its current plan, this would drop below $3.0 trillion by 2020. For the longer-term, the Fed has said its intention is to keep its balance sheet "appreciably below that seen in recent years but larger than before the financial crisis".

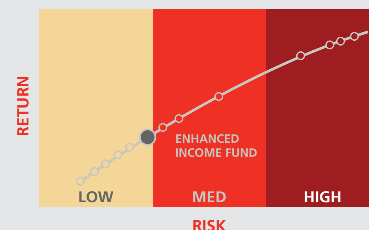
US Treasury bonds (USTs) posted small capital losses in Q4, while the US yield curve (the difference between short-term and 10-year yields) moved to its flattest in over 10 years. This perhaps reflects a view that while the Federal Reserve will continue to tighten policy next year, the peak in US rates will be well below that of previous cycles since inflation remains well contained. At quarter-end, the 10-year UST yield was trading around 2.4% from 2.3% at the end of Q3. For US corporate bonds, investment-grade bond spreads narrowed slightly over USTs, while high-yield spreads were roughly unchanged over the three months.

In the Eurozone, the region grew a stronger-than-expected 2.5% (q/q annualised) in Q3, up from a revised 2.3% in Q2, as the recovery became more broad-based across many euro-area countries, and helped by the ECB's ongoing easy monetary policy. Economic growth is now forecast at 2.2% y/y for 2017, the fastest in a decade. Despite the unemployment rate falling to a nearly nine-year low of 8.8%, inflation remained becalmed with CPI at 1.5% y/y in November. Meanwhile, the euro continued its appreciation in Q4 – the currency was the strongest performer against the US dollar in 2017, gaining 12.7% for the year as investors bet on accelerating Eurozone growth while the US business cycle aged. At its December meeting the ECB left interest rates on hold as expected, given subdued inflation. For the quarter, the Dow Jones Eurostoxx 50 (in US$) returned -0.8%, but 24.3% for 2017.

Meanwhile, the UK continued to face a Brexit-inspired dilemma, with uncertainty curtailing economic growth but fuelling inflation from the weaker pound. Although progress was finally made in Brexit negotiations during the quarter, Q3 GDP growth was only 1.5% (q/q annualised), while November CPI surprised to the upside at 3.1% y/y. The Bank of England opted to raise interest rates by 25bps in November, its first hike since 2007 - investors now expect no further hikes until late 2018. The FTSE 100 returned 6.0% (in US$) over the quarter and 22.6% for the year.

In China, Q3 GDP growth slowed marginally as expected, to 6.8% (q/q annualised) from 6.9% in Q2, dented by the government's attempts to rein in property market speculation and reduce debt. This is still above 2017's official 6.5% growth target, with factory output boosted by improving global trade. The equity market continued its remarkable performance with the MSCI China returning 7.6% in Q4: it was among the world's strongest markets in 2017 with a total return of 54.3%. Other emerging market (EM) assets posted strong returns in Q4 as risk-hungry investors continued to seek out EM equities. Overall, the MSCI Emerging Markets Index returned 7.5% in US$ for the quarter, and an impressive 37.3% in 2017.

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 382 087 249

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	X CLASS	D CLASS
1 year	8.2%	7.6%	8.7%	8.4%	8.8%
3 years	7.3%	7.1%	n/a	7.6%	7.9%
5 years	7.2%	6.5%	n/a	7.4%	7.8%
7 years	8.0%	7.1%	n/a	n/a	n/a
Since inception	8.6%	7.3%	7.5%	8.3%	8.5%

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

ASSET CLASS RETURNS	Q4 2017	2017
Global equity – MSCI World (US$) (Developed)	5.6%	22.4%
Global equity – MSCI Emerging Markets (US$)	7.5%	37.3%
Global bonds – Bloomberg Barclays Global Agg Bond Index (US$)	1.1%	7.4%
Global property – FTSE EPRA/NAREIT Global REIT (US$)	3.1%	6.8%
SA equity – FTSE/JSE All Share Index	7.4%	21.0%
SA bonds – BEASSA All Bond Index	2.2%	10.2%
SA listed property – SA Listed Property Index	8.3%	17.2%
SA inflation-linked bonds – JSE CILI Index	1.0%	2.9%
SA cash (STeFI Composite Index)	1.8%	7.5%

Sources: Prudential, Morningstar & Deutsche Securities

In commodities, the price of Brent crude jumped some 16% during the quarter to end the year at over US$66.50 per barrel, up nearly 18% for 2017 as a whole as OPEC and other producers successfully curbed supply in the latter half of the year and look set to extend production cuts through the end of 2018. Other commodity prices also gained ground in Q4, extending their strong gains over the year in line with accelerating global growth and a weaker dollar.

Despite the sluggish local economy, elevated political risk and further credit rating downgrades during the quarter, South African assets performed surprisingly strongly. Although bonds and listed property experienced sharp sell-offs after the revelation of SA's deteriorating fiscal position in October's Medium-Term Budget Policy Statement (MTBPS), they both managed a relief rally following Moody's postponement of its credit rating decision in late November, and saw even better gains in the "Ramaphosa rally" amid the post-ANC conference exuberance in December. Investors were keen to snap up the attractive yields on offer. The BEASSA All Bond Index returned 2.2% for the quarter and a strong 10.2% for the year. Inflation-linked bonds (Composite ILB Index) produced a more muted 1.0% for Q4 and 2.9% in 2017, while cash as measured by the STeFI Composite Index delivered 1.8% in the quarter and 7.5% for the year. Finally, SA listed property produced 8.3% in Q4, for an unexpectedly robust total return of 17.2% in 2017.

The quarter's political and credit ratings news managed to overshadow some of the fundamentals: SA's Q3 GDP growth was reported at 2.0% (q/q, annualised), with agriculture, mining and manufacturing the main drivers of the expansion. In the first nine months of 2017, the South African economy grew by 1.0% y/y. At the same time, November CPI eased to 4.6% y/y from 4.8% in October, helping underpin interest-rate-sensitive assets like bonds and listed property. Despite the improving inflation data, the SA Reserve Bank (SARB) opted to leave interest rates on hold over the quarter, citing upside risks to inflation from possible rand weakness, further downgrades and political uncertainty. However, the recent rand rally could mitigate the SARB's view, helping to ease inflationary pressures in 2018.

The rand also benefited from the December Ramaphosa rally, as well as the positively perceived Moody's reprieve. Despite Q4's high volatility, the local currency managed to appreciate 8.8% against the US dollar and 7.5% against the euro over the period. For the entire year it gained 10.1% versus the greenback and 1.9% versus UK sterling, but depreciated 2.2% against the robust euro.

In SA listed property, although benefiting from the improved inflation and interest rate outlook, deteriorating medium-term economic growth prospects in South Africa, as well as the credit rating downgrades, have increased the risks to the sector somewhat. We are comfortable maintaining our position in listed property, which we believe is trading around its fair value and priced to deliver attractive inflation-beating returns over the medium term.

In SA nominal bonds, valuations are on the cheap side of fair value at year end. This is despite the strong December Ramaphosa rally that saw 10-year yields fall (and valuations rise) from attractive levels of well over 9% to around 8.6% at year-end. However, post the Ramaphosa rally in December, we reduced the fund's SA Nominal bond position.

For inflation-linked bonds, we continue to hold this asset class and consider real yields as attractive even after the Ramaphosa rally.

The uncertainty around our fiscal policy implementation, governance standards and political risk will keep financial market volatility elevated in the months ahead.

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. ■

DISCLAIMER

Prudential Portfolio Managers Unit Trusts Ltd (Registration number: 1999/0524/06) is an approved CISCA management company (#29). Assets are managed by Prudential Investment Managers (South Africa) (Pty) Ltd, which is an approved discretionary Financial Services Provider (#45199). The Trustee's/Custodian details are: Standard Bank of South Africa Limited - Trustee Services & Investor Services. 20th Floor, Main Tower, Standard Bank Centre, Heerengracht, Cape Town. Collective Investment Schemes (unit trusts) are generally medium-to long-term investments. Past performance is not necessarily a guide to future investment performance. Unit trust prices are calculated on a net asset value basis. This means the price is the total net market value of all assets of the unit trust fund divided by the total number of units of the fund. Any market movements – for example in share prices, bond prices, money market prices or currency fluctuations - relevant to the underlying assets of the fund may cause the value of the underlying assets to go up or down. As a result, the price of your units may go up or down. Unit trusts are traded at the ruling forward price of the day, meaning that transactions are processed during the day before you or the Manager know what the price at the end of the day will be. The price and therefore the number of units involved in the transaction are only known on the following day. The unit trust fund may borrow up to 10% of the fund value, and it may also lend any scrip (proof of ownership of an investment instrument) that it holds to earn additional income. A Prudential unit trust fund may consist of different fund classes that are subject to different fees and charges. Where applicable, the Manager will pay your financial adviser an agreed standard ongoing adviser fee, which is included in the overall costs of the fund. A Collective Investment Schemes (CIS) summary with all fees and maximum initial and ongoing adviser fees is available on our website. One can also obtain additional information on Prudential products on the Prudential website. The Manager may, at its discretion, close your chosen unit trust fund to new investors and to additional investments by existing investors to make sure that it is managed in accordance with its mandate. It may also stop your existing debit order investment. The Manager makes no guarantees as to the capital invested in the fund or the returns of the fund. Excessive withdrawals from the fund may place the fund under liquidity pressure and, in certain circumstances; a process of ring fencing withdrawal instructions may be followed. The Fund may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks. The volatility of the fund may be higher and the liquidity of the underlying securities may be restricted due to relative market sizes and market conditions. The fund's ability to settle securities and to repatriate investment income, capital or the proceeds of sales of securities may be adversely affected for multiple reasons including market conditions, macro-economic and political circumstances. Further, the return on the security may be affected (positively or negatively) by the difference in tax regimes between the domestic and foreign tax jurisdictions. The availability of market information and information on any underlying sub-funds may be delayed. Fund prices are published daily on the Prudential website. These are also available upon request. The performance is calculated for the portfolio. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestment and dividend withholding tax.Purchase and repurchase requests must be received by the Manager by 13h30 SA time each business day. All online purchase and repurchase transactions must be received by the Manager by 10h30 (for all Funds) SA time each business day.

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL INFLATION PLUS FUND
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

MARKET OVERVIEW

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole. The longstanding rally looked set to continue into the new year amid ongoing optimism over the health of the global economy, still-subdued inflation, supportive monetary policies and bullish investor sentiment, given an additional fillip by the enactment of major corporate tax cuts in the US. The US Federal Reserve continued its very gradual tightening, the Bank of England hiked interest rates for the first time in a decade, and the European Central Bank (ECB) kept interest rates unchanged. Global bonds posted a muted return amid mixed sentiment over prospects for rising inflation and interest rates.

For South African investors it was a surprisingly positive quarter, with all local asset classes managing to post solid returns, especially in the wake of the rally sparked by market-friendly Cyril Ramaphosa's election as the new President of the ANC in December. Despite the installation of a divided ANC leadership committee with competing policy approaches, investors interpreted Ramaphosa's election as an opportunity for the country to introduce much-needed reforms, reduce corruption, and lift business and consumer sentiment. Greater prospects for improved fiscal responsibility also helped the credit rating outlook. Combined with Moody's credit rating reprieve in November, this more optimistic sentiment helped lower risk perceptions among both local and offshore investors, driving strong rallies in South African bonds and the rand. SA equities, although returning a respectable 7.4% for the quarter, were adversely affected in December by the collapse in the share prices of Steinhoff and its associated companies, counterbalanced partly by a rise in domestically oriented shares (including banks and retailers) post the ANC elective conference.

US stock markets again reached fresh record highs this quarter, with the Dow Jones Industrial Average approaching 25,000 at year-end and returning an exceptional 28.1% to investors for 2017. For Q4, the S&P 500 returned 6.6% (21.8% in 2017) and the Nasdaq 7.3% (33% in 2017, an amazing year thanks to its technology-heavy composition). The Bloomberg Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, returned 1.1% in the quarter, although much of this was driven by a weaker US dollar, which enhanced mediocre returns from non-US bond markets. It returned 7.4% for the year. At quarter-end, the 10-year UST yield was trading around 2.4% from 2.3% at the end of Q3. For US corporate bonds, investment-grade bond spreads narrowed slightly over USTs, while high-yield spreads were roughly unchanged over the three months.

For the quarter, the Dow Jones Eurostoxx 50 (in US$) returned -0.8%, but 24.3% for 2017. The FTSE 100 returned 6.0% (in US$) over the quarter and 22.6% for the year. Japanese stocks experienced their best year since 2013 on stronger corporate profits growth: the Nikkei 225 Index returned 12.1% over the quarter (in US$) and 25.7% for 2017. In China, the equity market continued its remarkable performance with the MSCI China returning 7.6% in Q4: it was among the world's strongest markets in 2017 with a total return of 54.3%.

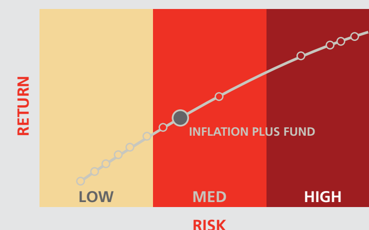
Other emerging market (EM) assets posted strong returns in Q4 as risk-hungry investors continued to seek out EM equities. Overall, the MSCI Emerging Markets Index returned 7.5% in US$ for the quarter, and an impressive 37.3% in 2017. This compared to 5.6% and 22.4%, respectively, from the MSCI World Index for developed markets. Among the larger EM equity markets in US$ terms for the year, South Korea's KOSPI returned 41.3%, the MSCI Turkey 39.1%, the MSCI India 38.8% and the MSCI South Africa 36.8% (helped by the stronger rand versus the US dollar).

In commodities, the price of Brent crude jumped some 16% during the quarter to end the year at over US$66.50 per barrel, up nearly 18% for 2017 as a whole as OPEC and other producers successfully curbed supply in the latter half of the year and look set to extend production cuts through the end of 2018. Other commodity prices also gained ground in Q4, extending their strong gains over the year in line with accelerating global growth and a weaker dollar. Palladium topped commodity gains in 2017 with a 57.8% price rise on the back of its increasing usage in vehicles, while platinum posted an annual gain of only 2.8% on oversupply concerns. Industrial metals reflected the higher global growth trend: aluminium was the second-best performer in 2017 at 32.4%, while copper and zinc both experienced 30.5% rises. Gold gained 13.5% for the year, largely on the back of North Korean tensions.

In South Africa, despite the sluggish local economy, elevated political risk and further credit rating downgrades during the quarter, assets performed surprisingly strongly. Although bonds and listed property experienced sharp sell-offs after the revelation of SA's deteriorating fiscal position in October's Medium-Term Budget Policy Statement (MTBPS), they both managed a relief rally following Moody's postponement of its credit rating decision in late November, and saw even better gains in the "Ramaphosa rally" amid the post-ANC conference exuberance in December.

Investors were keen to snap up the attractive yields on offer. The BEASSA All Bond Index returned 2.2% for the quarter and a strong 10.2% for the year. Inflation-linked bonds (Composite ILB Index) produced a more muted 1.0% for Q4 and 2.9% in 2017, while cash as measured by the STeFI Composite Index delivered 1.8% in the quarter and 7.5% for the year. Finally, SA listed property produced 8.3% in Q4, for an unexpectedly robust total return of 17.2% in 2017.

RISK/RETURN PROFILE:



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

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

OBJECTIVE (BEFORE FEES):
CPI+5% p.a. over a rolling 3-year period

INCEPTION DATE:
1 June 2001

FUND SIZE:
R37 794 934 418

AWARDS:
Raging Bull: 2013
Morningstar: 2015

ANNUALISED PERFORMANCE	A CLASS	OBJECTIVE#	T CLASS	X CLASS	B CLASS
1 year	10.3%	8.0%	10.9%	10.6%	11.1%
3 years	7.5%	8.7%	n/a	7.8%	8.3%
5 years	9.9%	8.8%	n/a	10.2%	10.7%
7 years	11.4%	9.0%	n/a	n/a	12.2%
10 years	10.3%	9.4%	n/a	n/a	11.1%
Since inception	13.0%	9.5%	7.2%	11.8%	13.0%

Objective (After A Class Fees) over a rolling 3-year period. Fee adjustment to gross Fund Objective for different classes: A class -1.7%, T class -1% , X class -1.4% , B c

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

ASSET CLASS RETURNS	Q4 2017	2017
Global equity – MSCI World (US$) (Developed)	5.6%	22.4%
Global equity – MSCI Emerging Markets (US$)	7.5%	37.3%
Global bonds – Bloomberg Barclays Global Agg Bond Index (US$)	1.1%	7.4%
Global property – FTSE EPRA/NAREIT Global REIT (US$)	3.1%	6.8%
SA equity – FTSE/JSE All Share Index	7.4%	21.0%
SA bonds – BEASSA All Bond Index	2.2%	10.2%
SA listed property – SA Listed Property Index	8.3%	17.2%
SA inflation-linked bonds – JSE CILI Index	1.0%	2.9%
SA cash (STeFI Composite Index)	1.8%	7.5%

Sources: Prudential, Morningstar & Deutsche Securities

SA equities, meanwhile, were helped by global enthusiasm. For 2017 as a whole, the ALSI had a remarkable year given the poor local fundamentals, producing a total return of 21.0%, most of which came in the second half. Among the sectors, it was Industrials that returned the most with 22.5% (led by Naspers with a total return of 72%), while Financial stocks delivered 20.6%, listed Property 17.2% and Resources 16.8%. Excluding Naspers, the ALSI would have returned only around 13% for the year.

The market suffered a significant drop in early December on the back of the plunge in the share prices of Steinhoff and associated companies such as Steinhoff Africa Retail (STAR) and Brait. This was partially offset by the Ramaphosa rally, led by retail and banking stocks, but rand strength hit the share prices of those companies with significant offshore earnings, including industrial and resources counters. For the quarter, the ALSI returned 7.4%, thanks to a 16.0% return from Financials and a 22% return from retailers, both boosted by the stronger rand and an improved local outlook. Resources returned 3.6% and Industrials as a sector delivered 4.7%, with Property returning 8.3%.

Finally, the rand also benefited from the December Ramaphosa rally, as well as the positively perceived Moody's reprieve. Despite Q4's high volatility, the local currency managed to appreciate 8.8% against the US dollar and 7.5% against the euro over the period. For the entire year it gained 10.1% versus the greenback and 1.9% versus UK sterling, but depreciated 2.2% against the robust euro.

PERFORMANCE

The fund returned 3.3% (after fees) for the fourth quarter of 2017 and has returned 10.3% for the 12-month period ending 31 December 2017, compared against expected inflation for the year of 5.3% (December's CPI data hasn't been released at the time of writing). The fund has delivered a return of 13.0% per annum since inception (after fees), compared to its after-fee objective of 9.5% per annum over the same period.

To 31 December 2017 it retains its top-quartile or better performance over all annual periods to 10 years (except 2 years), according to Morningstar. Among the largest contributors to returns for the quarter were the fund's exposure to SA equities (particularly Naspers, banks, retail and listed property shares), and to a lesser extent SA bonds and ILBs. The fund's overall international exposure detracted from value due to the appreciation of the rand over the quarter, although its underweight positioning in international fixed income relative to international equity added to value.

STRATEGY AND OUTLOOK

In **global fixed income**, despite recent rises in government bond yields, they continue to trade at very low levels (and high valuations) historically, and remain at risk to rising interest rates in the US and UK, and increasingly in Europe as well. We continue to be underweight global sovereign bonds and underweight duration to reduce interest rate risk, preferring to hold investment-grade US and European corporate bonds.

For **global equities**, the sharp rallies seen over the past seven quarters in many countries has been driven in part by a re-rating of the MSCI All Country World Index, but strong corporate earnings growth has kept the Index within its fair value range. Against the backdrop of upside surprises to broad global growth, we see better value in many regions compared to South Africa, which is why we continue to be overweight global equities. Our current global equity positioning reflects a preference for cheaper areas where fundamentals are encouraging and valuations remain attractive, including Europe, Japan, the global financial sector and smaller holdings in selected emerging markets such as South Korea, Indonesia and Turkey. These positions are financed by an underweight in US and Canadian equities and in global bonds.

South African equities became somewhat more expensive in Q4 2017 despite losing some ground later in the quarter: the FTSE/JSE ALSI 12-month forward P/E rose to around 15.4X at quarter-end from around 14.6X in Q3. This is modestly expensive compared to its long-term fair value, but excluding Naspers (which is now over 20% of the market and which should be valued relative to global technology stocks), the market is close to fair value and priced to deliver attractive medium-term returns. In the context of the low-equity Inflation Plus Fund's 40% total equity exposure limit (a limit set by the ASISA category), we see better opportunities offshore. Consequently we continue to be slightly underweight SA equities in the Prudential Inflation Plus Fund and overweight global equities, with total equity exposure close to the maximum allowed.

Our individual equity exposure is similar to the previous quarter. During the year we held a significant underweight exposure to Steinhoff due to our long-standing concerns over the business and its balance sheet. We sold all of our Steinhoff holdings on the morning following the resignation of its CEO. Currently, the fund holds stocks with ample foreign currency earnings like Naspers, British American Tobacco, Richemont, Anglo American and BHP Billiton – the latter two representing lower risk to commodity price weakness given their diversification. We also hold non-mining resources stocks like Sappi, as well as international container transport group Trencor, which has upside to improving global trade trends. We remain overweight in well-priced and high-yielding Financials including Old Mutual, Investec, Standard Bank and FirstRand, which have offered relatively high dividend yields while also providing a valuation cushion in the event of further credit rating downgrades. In retrospect, these financial companies weathered 2017's volatility well. Offsetting this overweight position, we have chosen to remain underweight in Retail stocks given the challenging local consumer environment, although prospects here may be improving thanks to lower inflation improving real incomes and the improving political environment lifting confidence.

In **SA listed property,** we have a neutral exposure in the Inflation Plus Fund. Fundamentals for the sector deteriorated somewhat, particularly for the retail and office sectors and valuations began to look more stretched when compared to inflation-linked bonds. Rand strength is also likely to reduce the future earnings (in rand terms) of the offshore property companies which now comprise 40% of the SA market. We are comfortable maintaining a neutral position in listed property, which we believe is trading around long-term fair value at year-end, but still priced to deliver attractive inflation-beating returns over the medium term. A domestic macroeconomic recovery and an ongoing global growth upswing would both assist in providing a favourable backdrop for this asset class in 2018.

In **SA nominal bonds**, we are modestly overweight as valuations are on the cheap side of fair value at year end. This is despite the strong December Ramaphosa rally that saw 10-year yields fall (and valuations rise) from attractive levels of well over 9% to around 8.6% at year-end. During the quarter we added to our bond position in the wake of their sell-off following the MTBPS in November, and reduced this position after the December rally. We continue to prefer longer-dated government bonds due to the more attractive yields on offer, and are comfortable with the compensation bonds offer for the extra risk involved when considering further downgrade prospects.

For **inflation-linked bonds**, we continue to be neutrally positioned in this asset class. Real yields are attractive, even after the Ramaphosa rally, but better value exists elsewhere – in long-dated nominal bonds and equities. Our funds were largely underweight this asset class during 2017 until later in Q3, when their valuation fell to more attractive levels relative to nominal bonds (amid the improved inflation outlook). At that point we took advantage of this to buy more ILBs and moved to a neutral exposure. ■

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL BALANCED FUND
31 DECEMBER 2017

QUARTERLY COMMENTARY

MULTI-ASSET

PERFORMANCE

The fund gained 3.2% over the quarter, bringing the calendar year return to 11.8% (both net of fees). All domestic asset classes enjoyed positive gains, while all the international asset classes suffered losses in rand terms as the rand strengthened sharply over the quarter. The main contributor to fund returns was the strong return from domestic equities – in particular the strong gains enjoyed by the fund's banking and retail shares. The major contributor to the fund's relative return versus its benchmark was its large underweight exposure to Steinhoff, as the share's price collapsed in December, falling 92%.

MARKET OVERVIEW

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole. The longstanding rally looked set to continue into the new year amid ongoing optimism over the health of the global economy, still-subdued inflation, supportive monetary policies and bullish investor sentiment, given an additional fillip by the enactment of major corporate tax cuts in the US. The US Federal Reserve continued its very gradual tightening, the Bank of England hiked interest rates for the first time in a decade, and the European Central Bank (ECB) kept interest rates unchanged. Global bonds posted a muted return amid mixed sentiment over prospects for rising inflation and interest rates.

Despite the sluggish local economy, elevated political risk and further credit rating downgrades during the quarter, South African assets performed surprisingly strongly. Although bonds and listed property experienced sharp sell-offs after the revelation of SA's deteriorating fiscal position in October's Medium-Term Budget Policy Statement (MTBPS), they both managed a relief rally following Moody's postponement of its credit rating decision in late November, and saw even better gains in the "Ramaphosa rally" amid the post-ANC conference exuberance in December. Investors were keen to snap up the attractive yields on offer. The BEASSA All Bond Index returned 2.2% for the quarter and a strong 10.2% for the year. Inflation-linked bonds (Composite ILB Index) produced a more muted 1.0% for Q4 and 2.9% in 2017, while cash as measured by the STeFI Composite Index delivered 1.8% in the quarter and 7.5% for the year. Finally, SA listed property produced 8.3% in Q4, for an unexpectedly robust total return of 17.2% in 2017.

Equities, meanwhile, were helped by global enthusiasm over the quarter: the FTSE/JSE All Share Index hit new record highs in November, rising briefly to 61,299 points before retracing about 3% to close December at around 59,500 points. The market suffered a significant drop in early December on the back of the plunge in the share prices of Steinhoff and associated companies such as Steinhoff Africa Retail (STAR) and Brait. This was partially offset by the Ramaphosa rally, led by retail and banking stocks, but rand strength hit the share prices of those companies with significant offshore earnings, including industrial and resources counters.

For the quarter, the ALSI returned 7.4%, thanks to a 16.0% return from Financials and a 22% return from retailers, both boosted by the stronger rand and an improved local outlook. Resources returned 3.6% and Industrials as a sector delivered 4.7%, with Property returning 8.3%. For 2017 as a whole, the ALSI had a remarkable year given the poor local fundamentals, producing a total return of 21.0%, most of which came in the second half.

The quarter's political and credit ratings news managed to overshadow some of the fundamentals: SA's Q3 GDP growth was reported at 2.0% (q/q, annualised), with agriculture, mining and manufacturing the main drivers of the expansion. At the same time, November CPI eased to 4.6% y/y from 4.8% in October, helping underpin interest-rate-sensitive assets like bonds and listed property. Despite the improving inflation data, the SA Reserve Bank (SARB) opted to leave interest rates on hold over the quarter, citing upside risks to inflation from possible rand weakness, further downgrades and political uncertainty. The rand also benefited from the December Ramaphosa rally, as well as the positively perceived Moody's reprieve. Despite Q4's high volatility, the local currency managed to appreciate 8.8% against the US dollar and 7.5% against the euro over the period. For the entire year it gained 10.1% versus the greenback and 1.9% versus UK sterling, but depreciated 2.2% against the robust euro.

STRATEGY AND OUTLOOK

The fund is underweight global bonds and global cash, and overweight global equities, with the latter offering attractive valuations in certain markets and much higher potential returns over the medium term. In global fixed income, despite recent rises in government bond yields, they continue to trade at very low levels (and high valuations) historically, and remain at risk to rising interest rates in the US and UK, and increasingly in Europe as well. We continue to be underweight global sovereign bonds and underweight duration to reduce interest rate risk, preferring to hold investment-grade US and European corporate bonds.

For global equities, the strong rallies seen over the past seven quarters in many countries has been driven in part by a re-rating of the MSCI All Country World Index, but strong corporate earnings growth has kept the Index within its fair value range. Against the backdrop of upside surprises to broad global growth, we see better value in many regions compared to South Africa, which is why we continue to be overweight global equities. Our current global equity positioning reflects a preference for cheaper areas where fundamentals are encouraging but valuations remain attractive, including Europe, Japan, the global financial sector and smaller holdings in selected emerging markets such as Korea, Turkey and Indonesia. These positions are financed by an underweight in US equities and in global bonds.

South African equities became somewhat more expensive in Q4 2017 despite losing some ground later in the quarter: the FTSE/JSE ALSI 12-month forward P/E rose to around 15.4X at quarter-end from around 14.6X in Q3. This is modestly expensive compared to its long-term fair value, but excluding Naspers (which is now over 20% of the market and which should be valued relative to global technology stocks), the market is still at fair value and priced to deliver attractive medium-term returns. As such we are overweight local equity.

During the year we held an underweight exposure to Steinhoff due to our long-standing concerns over numerous issues. We sold all of our Steinhoff holdings on the morning following the resignation of its CEO. Currently, our portfolios hold stocks with ample foreign currency earnings like Naspers, British American Tobacco, Richemont, Anglo American and BHP Billiton – the latter two representing lower risk to commodity price weakness given their diversification. We also hold non-mining resources stocks like Sappi, as well as international container transport group Trencor, which has upside to improving global trade trends. We remain overweight in well-priced and high-yielding Financials including Old Mutual, Investec, Standard Bank and FirstRand, which have offered relatively high dividend yields while also providing a valuation cushion in the event of further credit rating downgrades. In retrospect, these financial companies weathered 2017's volatility well. Offsetting this overweight position, we have chosen to remain underweight in Retail stocks given the challenging local consumer environment.

In SA listed property, we have a neutral exposure in our multi-asset portfolios. Although benefiting from the improved inflation and interest rate outlook, deteriorating medium-term economic growth prospects in South Africa, as well as the credit rating downgrades, have increased the risks to the sector somewhat. We are comfortable maintaining a neutral position in listed property, which we believe is trading around its fair value and priced to deliver attractive inflation-beating returns over the medium term.

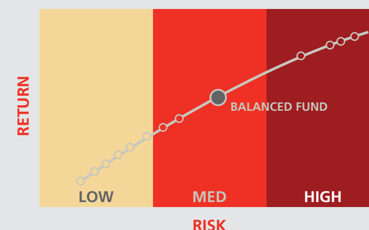
In SA nominal bonds, we are modestly overweight as valuations are on the cheap side of fair value at year end. This is despite the strong December Ramaphosa rally that saw 10-year yields fall (and valuations rise) from attractive levels of well over 9% to around 8.6% at year-end. During the quarter we added to our bond position in the wake of their sell-off following the MTBPS in November, and reduced this position after the December rally. We continue to prefer longer-dated government bonds due to the more attractive yields on offer, and are comfortable with the compensation bonds offer for the extra risk involved when considering further downgrade prospects. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	X CLASS	B CLASS
1 year	11.8%	10.0%	12.4%	15.5%	12.6%
3 years	8.0%	6.3%	n/a	8.3%	8.8%
5 years	11.8%	9.2%	n/a	12.1%	12.6%
7 years	12.3%	9.6%	n/a	n/a	13.2%
10 years	10.5%	8.3%	n/a	n/a	11.4%
Since inception	14.2%	12.3%	7.5%	11.9%	14.7%

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

ASSET CLASS RETURNS	Q4 2017	2017
Global equity – MSCI World (US$) (Developed)	5.6%	22.4%
Global equity – MSCI Emerging Markets (US$)	7.5%	37.3%
Global bonds – Bloomberg Barclays Global Agg Bond Index (US$)	1.1%	7.4%
Global property – FTSE EPRA/NAREIT Global REIT (US$)	3.1%	6.8%
SA equity – FTSE/JSE All Share Index	7.4%	21.0%
SA bonds – BEASSA All Bond Index	2.2%	10.2%
SA listed property – SA Listed Property Index	8.3%	17.2%
SA inflation-linked bonds – JSE CILI Index	1.0%	2.9%
SA cash (STeFI Composite Index)	1.8%	7.5%

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:

R18 224 899 543

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL ENHANCED SA PROPERTY TRACKER FUND
31 DECEMBER 2017

QUARTERLY COMMENTARY | **PROPERTY**

PERFORMANCE

The fund recorded a positive return of 6.0% (net of fees) for the quarter while the SA Listed Property (SAPY) index increased by 8.3%. The fund's 2.3% underperformance versus the benchmark over this period was largely attributable to the fund's 2.5% overweight in Arrowhead (AWA) which came out with a 13% negative distribution growth surprise in November. Subsequently the stock was down by 18% by the end of November which thus detracted -1.0% from performance given the overweight position.

Further negative performance resulted from the fund's overweight position in Hospitality (HPB) of just under 1%. In November HPB released interim results which were on the face of it quite weak. As a result of the subsequent share price underperformance the overweight contributed -0.29% to performance over the quarter.

Both the AWA and HPB positions are examples of the active stock selection of our fundamental strategy of holding excess weight in higher-yielding stocks. Despite periods where cheap stocks get cheaper we believe our valuation based approach will deliver outperformance over the longer-term.

Over the past year the fund returned 14.4% (net of fees), lagging the benchmark by 2.7%. The rolling 12 months performance of the fund ranked it 21st out of 39 funds in the ASISA South African Real Estate General peer group.

The 10-year track record of the fund ranks it 6th out of its peers, with the fund having underperformed the benchmark (after fees) by 0.1% over this period.

MARKET COMMENTARY

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole.

In the US, the latest GDP data (Q3) showed growth accelerating to 3.3% (q/q annualised) from 3.1%, propelled by higher business investment and rising inventories, while consumer confidence reached a 17-year high in November. This marked the 32nd consecutive quarter of US economic expansion since the 2009 recession, the third longest since 1945. Meanwhile, consumer inflation remained at moderate levels: November CPI came in at 2.2% y/y, in line with expectations, with the small rise from October's 2.0% y/y attributable mainly to rising oil prices.

Taking this expansion together with full employment and the large corporate tax cuts passed by the US legislature in December, analysts expect inflation to become more problematic in 2018 – market consensus is for four 25bp Fed rate hikes in the new year following its 25bp increase in December.

For South African investors it was a surprisingly positive quarter, with all local asset classes managing to post solid returns, especially in the wake of the rally sparked by market-friendly Cyril Ramaphosa's election as the new President of the ANC in December. Despite the installation of a divided ANC leadership committee with competing policy approaches, investors interpreted Ramaphosa's election as an opportunity for the country to introduce much-needed reforms, reduce corruption, and lift business and consumer sentiment.

Greater prospects for improved fiscal responsibility also helped the credit rating outlook. Combined with Moody's credit rating reprieve in November, this more optimistic sentiment helped lower risk perceptions among both local and offshore investors, driving strong rallies in South African bonds and the rand.

Although bonds and listed property experienced sharp sell-offs after the revelation of SA's deteriorating fiscal position in October's Medium-Term Budget Policy Statement (MTBPS), they both managed a relief rally following Moody's postponement of its credit rating decision in late November, and saw even better gains in the "Ramaphosa rally" amid the post-ANC conference exuberance in December. Investors were keen to snap up the attractive yields on offer. The BEASSA All Bond Index returned 2.2% for the quarter and a strong 10.2% for the year. Inflation-linked bonds (Composite ILB Index) produced a more muted 1.0% for Q4 and 2.9% in 2017, while cash as measured by the STeFI Composite Index delivered 1.8% in the quarter and 7.5% for the year. Finally, SA listed property produced 8.3% in Q4, for an unexpectedly robust total return of 17.2% in 2017.

The quarter's political and credit ratings news managed to overshadow some of the fundamentals: SA's Q3 GDP growth was reported at 2.0% (q/q, annualised), with agriculture, mining and manufacturing the main drivers of the expansion. In the first nine months of 2017, the South African economy grew by 1.0% y/y. At the same time, November CPI eased to 4.6% y/y from 4.8% in October, helping underpin interest-rate-sensitive assets like bonds and listed property. Despite the improving inflation data, the SA Reserve Bank (SARB) opted to leave interest rates on hold over the quarter, citing upside risks to inflation from possible rand weakness, further downgrades and political uncertainty. However, the recent rand rally could mitigate the SARB's view, helping to ease inflationary pressures in 2018.

In SA listed property, we maintained a neutral exposure in our multi-asset funds through the quarter and into January. Yields are currently considered to be at fair levels following a slight sell off post year end. 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, appropriate compensation for the risk involved.

Actual delivered growth in distributions per share for the major listed property companies averaged 11.8% for the last 6 months' reporting cycle.

We estimate that one-year forward earnings forecasts for the SAPY, excluding developers, contracted by just under 1% on an annualized basis over the quarter. This implies slight downgrades to forecasts for the sector (relative to expectations) given that consensus forecasts have been for growth rates of the order of 9.2%.

Within the major listed property sectors, retail remains under pressure as a result of consumer spending headwinds and low consumer confidence. Retail is also affected by increased supply of retail space contributing to the decrease in trading density growth rates (turnover/retail space). The office sector was the weakest of the sectors due to corporate consolidation and low business confidence as well as an increase in supply in key nodes. The weak office sector had a particularly negative impact on Arrowhead which is forecasting negative distribution growth rate for 2018. The industrial sector has however shown resilience.

Results from Octodec and SA Corporate with exposure to the residential property sector experienced downward pressure due to an increase in competition and higher residential vacancies.

STRATEGY AND OUTLOOK

Listed property valuations moved to moderately expensive levels during the quarter, while the earnings outlook deteriorated slightly. 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 rating/valuation of property), comfortably above inflation and, we believe, ample compensation for the risk involved. Even with the market pricing in a de-rating of around 2%, the medium-term prospective return would be approximately 14% p.a.

We estimate that one-year forward earnings forecasts for the SAPY, excluding developers, grew by 3.4% on an annualised basis over the quarter. This implies slight downgrades to forecasts for the sector (relative to expectations), given that consensus forecasts have been for growth rates of the order of 9.3%.

As prudent valuation-based investment managers we know how important it is to maintain a broadly diversified portfolio in uncertain conditions, and stay invested in growth assets like equities and listed property through the current low-return market cycle, to build a successful investment portfolio over the long term. We will continue to take advantage of the opportunities created to buy assets at attractive valuations where the risks are appropriate.

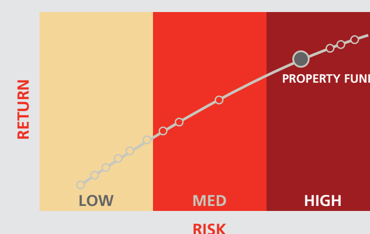
In the absence of a material de-rating in the market's valuation, listed property is priced to comfortably deliver double-digit returns over the medium term, well above inflation.

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 7.4%. This yield exceeded a combination of local and offshore 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	14.4%	17.2%	14.5%	14.6%
3 years	11.6%	11.7%	n/a	11.7%
5 years	13.9%	13.9%	n/a	14.1%
7 years	15.8%	16.0%	n/a	16.0%
10 years	14.8%	14.9%	n/a	n/a
Since inception	16.6%	16.9%	7.9%	17.2%

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

RISK/RETURN PROFILE:



RISK

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:

R7 737 817 142

AWARDS:

Morningstar/Standard & Poor's: 2011

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL DIVIDEND MAXIMISER FUND
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

PERFORMANCE

The fund produced a return of 5.3% for the three months ended December 2017, underperforming the average of the general equity funds by 0.3% for the same period. For the year ended December 2017, the Prudential Dividend Maximiser Fund outperformed the average of the general equity funds by 2.3% and returned a total return of 15.1%.

MARKET OVERVIEW

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole. The longstanding rally looked set to continue into the new year amid ongoing optimism over the health of the global economy, still-subdued inflation, supportive monetary policies and bullish investor sentiment, given an additional fillip by the enactment of major corporate tax cuts in the US. Global equity markets have been finding very good support as opposed to global bonds which posted a muted return. We are of the view that global equity markets (and emerging markets in particular) look like a much better prospect than global bonds. While equity markets have risen substantially, we think that this has been supported by good earnings and dividend growth. We expect earnings and dividends to continue growing strongly in the year ahead and remain overweight equities in South Africa and globally.

For South African investors it was a surprisingly positive quarter, with all local asset classes managing to post solid returns, especially in the wake of the rally sparked by market-friendly Cyril Ramaphosa's election as the new President of the ANC in December. Investors interpreted Ramaphosa's election as an opportunity for the country to introduce much-needed reforms, reduce corruption, and lift business and consumer sentiment.

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 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 aim to continue building risk-cognisant portfolios that seek to add value through stock selection relative to their benchmarks.

STRATEGY AND POSITIONING

In the last quarter, the fund's South African holdings had a very strong quarter and outperformed the benchmark substantially. This performance was offset by the translation of the foreign holdings of the fund into rands as a result of the rand strength in the last month of the year.

The fund's dual focus of buying undervalued companies with strong cash flows and dividends, put it in good stead during the last quarter. Our substantial underweight positions to Steinhoff, Aspen and EOH were the strongest contributors to relative performance during the quarter. We have owned no or very small amounts of these companies over the last decade due to the poor dividend growth and dividend yields. All these companies have been very acquisitive over time and have exhibited relatively poor dividend yields. Steinhoff in particular fell substantially due to concerns around revenue recognition and the overvaluation of assets.

Your fund's underweight position to Mondi Paper was also a strong contributor to performance. This is a company we regard highly as it has been able to grow its cash flows and earnings strongly over many years despite being faced with an industry where volume growth for their paper and cardboard products is either negative or very low. We sold our holdings in this company over the last year as we thought it had reached optimal margins and an optimal valuation. We continue to think that this company has the ability to generate strong cash flows and may buy back into this company in the future in the event that valuation levels become more reasonable.

The largest detractor from performance over the quarter was the fund's offshore investments. Your fund's offshore overweight position to global banks and leasing companies, which we think are exceptionally cheap, continued to perform in USD, but when translated to rands, underperformed.

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 attractive and currently over 25% of the fund is directly invested offshore across various markets.

OUTLOOK

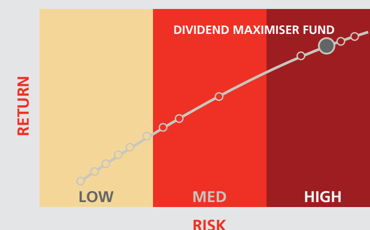
On market valuations, we currently view the market in South Africa as being fair value to undervalued. While we have been cautious regarding dividend growth in the South African market over the last five years, we now have more conviction that earnings and dividends should show a return to growth. This growth in dividends is based mainly on a return to more normal profit margins amongst the mining companies and related industries. We still consider some offshore equity markets to be relatively undervalued and attractive, and therefore maintain the fund's offshore exposure. We have, in addition, allocated some capital to the rest of Africa where we think dividends could show excellent growth over the next five years, particularly in Nigeria and Egypt.

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	15.1%	12.8%	15.4%	15.5%
3 years	7.5%	5.5%	n/a	8.0%
5 years	11.7%	9.1%	n/a	12.2%
7 years	12.3%	10.0%	n/a	12.8%
10 years	11.5%	8.5%	n/a	12.0%
Since inception	17.6%	14.4%	6.4%	12.1%

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 923 355 837

AWARDS:

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

DISCLAIMER
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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL EQUITY FUND
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

PERFORMANCE

The fund produced a return of 6.6% for the three months ending December 2017, outperforming the average of the general equity funds by 0.9% over the same period. This pleasing performance in the final quarter, contributed to the Prudential Equity Fund outperforming its benchmark by 3.6% over the full year, with a total return for 2017 of 16.4% net of fees.

MARKET OVERVIEW

In South Africa, the performance of the local market in December was dominated by two key events – the outcome of the ANC elective conference and the disclosure of financial irregularities at Steinhoff.

The emergence of the market's preferred candidate, Cyril Ramaphosa, as the new ANC president, together with what appears to be a party faction-neutral "top six" leadership body of the ANC, led to a strong relief rally and ignited key market indicators. The rand retraced its pre-conference weakness, rallying from levels of around R13,60/$ to end the year at R12.37/$, while domestic bond yields moved lower and both the domestic bank and retail shares rallied to record levels. The market interpreted Ramaphosa's election as an opportunity for the ruling party to introduce much needed policy reforms, address corruption and drive improved business and consumer confidence.

Against this backdrop, the announcement from Steinhoff of a delay in the release of its results, the resignation of its CEO Markus Jooste, and the appointment of forensic auditors to investigate accounting irregularities, sent the stock plummeting by over 90% in a day.

STRATEGY AND POSITIONING

In the final quarter, the fund's South African holdings delivered strong price gains, with some key positions outperforming the benchmark. However, the strong contribution from the domestic stocks was partially offset by the impact of December's rand strength on the translation of the fund's foreign assets.

A key contributor to performance, both over the quarter and for the year, was the fund's underweight position in Steinhoff. Prudential has long held a well-publicised negative view on Steinhoff, with key concerns around the group's highly acquisitive strategy, poor quality earnings, extraordinarily low tax rate and over-leveraged balance sheet. We have long maintained a significant underweight to the stock, and despite the collapse in Steinhoff's share price, see no merit to speculatively add to our current zero holding in the stock.

In addition to Steinhoff, the fund's holdings in Astral Foods, Exxaro and The Foschini Group all contributed positively to the performance over the quarter.

The key detractors to performance for the quarter came from the fund's holding in the offshore domiciled Prudential Global Equity Fund, as well as the position in Naspers, which were both negatively impacted by the translation effect of the stronger rand. In addition, the fund's underweight position to the general retail sector detracted from performance over the quarter, with Mr Price Group, a stock in which the fund has no holding, one of the largest relative detractors.

Synchronised global growth continued to spur demand for commodities, and the price of Brent crude jumped some 16% during the quarter to end the year at over US$66.50 per barrel, up nearly 18% for 2017. OPEC and other producers successfully curbed supply in the latter half of the year and look set to extend production cuts through the end of 2018. Sasol's valuation remains sensitive to both the exchange rate and the international price of oil. With the latter looking more stable, the fund has during the quarter closed an underweight position in Sasol. As we look ahead to 2019, Sasol's capex spend will have peaked, and the resulting cash flow from key projects will start to come on stream, enabling Sasol to pay down debt.

We would like to remind our investors that when investing in the JSE they are not only buying local companies exposed to the SA economy, but also shares in globally competitive companies that happen to be listed on the local exchange, but derive little, if any earnings from South Africa, such as British American Tobacco, Naspers, and Billiton. The Prudential Equity Fund, in addition to owning a selection of these local listed global companies, has chosen to allocate 20% of the fund directly offshore, primarily by holding units in the Prudential Global Equity Fund.

OUTLOOK

On market valuations, we currently view the market in South Africa as trading around fair value and offering investors an acceptable earnings yield.

We acknowledge that local banks and domestic consumer stocks have rallied hard, with current prices discounting market optimism for the potential improvement in the underlying economy. While it appears the earnings downgrade cycle may well have bottomed for these sectors, we remain sceptical about the prospect for any quick fix or recovery for our domestic economy. We still place high odds on the likelihood Moody's will downgrade South African sovereign bonds and remain concerned about funding needs of SOEs, in particular Eskom. We have, as a result, scaled back the fund's bank overweight position while retaining an underweight position in the general retail stocks given their current elevated ratings.

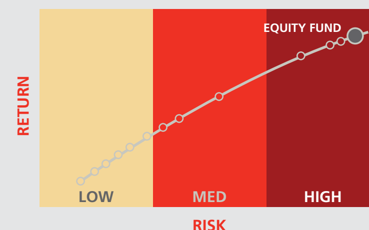
The outlook for diversified mining stocks remains positive given the prevailing commodity prices, with further earnings upgrades expected despite the stronger rand. In addition, quality rand hedges such as British American Tobacco look materially undervalued and should provide some protection in the event that domestic fiscal challenges result in a weakening of the rand from current levels.

We are confident we have managed to construct a diversified portfolio of attractively priced shares, which in aggregate is cheaper than owning the benchmark, without foregoing the ability to deliver underlying earnings in-line with that of the market. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	16.4%	12.8%	17.0%
3 years	8.1%	5.5%	8.6%
5 years	12.5%	9.1%	12.9%
7 years	13.1%	10.0%	13.6%
10 years	11.6%	8.5%	12.1%
Since inception	17.7%	14.4%	12.8%

Inception date B Class: 2 January 2007

RISK/RETURN PROFILE:



RISK

FUND MANAGERS:

Chris Wood, Johny Lambridis and Simon Kendall

ASISA CATEGORY:

South African - Equity - General

BENCHMARK:

ASISA South African - Equity - General Category Mean

INCEPTION DATE:

2 August 1999

FUND SIZE:

R2 994 996 764

AWARDS:

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

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL CAUTIOUS MANAGED FUND OF FUNDS
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL MULTI-ASSET

MARKET OVERVIEW

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole. The longstanding rally looked set to continue into the new year amid ongoing optimism over the health of the global economy, still-subdued inflation, supportive monetary policies and bullish investor sentiment, given an additional fillip by the enactment of major corporate tax cuts in the US.

The US Federal Reserve continued its very gradual tightening, the Bank of England hiked interest rates for the first time in a decade, and the European Central Bank (ECB) kept interest rates unchanged. Global bonds posted a muted return amid mixed sentiment over prospects for rising inflation and interest rates. US and German yield curves flattened, while credit, in particular investment grade outside of Europe, performed strongly.

The rand appreciated 8.8% against the US dollar, 7.5% against the euro and 8.2% against the pound over the quarter. For the year, the rand gained 10.1% versus the greenback and 1.9% versus UK sterling, however depreciated 2.2% against the euro.

PERFORMANCE

The fund returned 3.2% in US dollar terms for the quarter. Given the strong performance of the rand relative to the US dollar, the fund returned -5.9% in rand terms, outperforming its benchmark (the average return of the ASISA Global Multi-Asset Low Equity sector) by 0.8% as it generated -6.6%.

For the year, the fund earned 12.7% in US dollar terms. In rand terms, the fund returned 1.3% for the year compared to the benchmark's -2.7% over the same period.

The current economic environment worked well for the portfolio's positioning in favour of risk assets. Outperformance in relation to the benchmark is attributable to the portfolio's overweight in equities and underweight in fixed income.

POSITIONING

The portfolio is positioned broadly overweight equity versus underweight bonds. This reflects the fund manager's view that the size of the equity risk premium remains the most obvious opportunity on offer across the global investment landscape today.

STRATEGY AND OUTLOOK

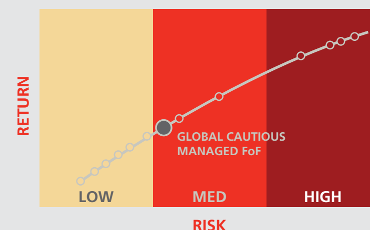
The fund is overweight equities and underweight bonds. This reflects the view that the size of the equity risk premium (ERP) remains the most obvious opportunity on offer across the global investment landscape today.

Despite recent rises in government bond yields, they continue to trade at very low levels (and high valuations) historically, and remain at risk to rising interest rates in the US and UK, and increasingly in Europe as well. We continue to be underweight global sovereign bonds as at these overvalued levels, these assets look vulnerable. However, we still see value in some emerging market bonds on elevated levels of real yield.

ERP remains compelling. This is because, despite the positive macroeconomic picture, investor sentiment remains somewhat pessimistic, although to a much lesser extent than 12 months ago. We still consider that, outside of the US, equity markets generally represent fair value, because economic fundamentals have improved in tandem with the rise in prices that has occurred. Nonetheless, we remain disciplined in terms of valuation and portfolio construction, identifying those cheaper markets where there is considerable upside and where less optimism is already priced in. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	1.3%	-2.7%	1.6%
3 years	5.6%	4.8%	5.9%
5 years	10.4%	9.8%	n/a
7 years	11.5%	11.1%	n/a
10 years	6.1%	6.1%	n/a
Since inception	7.3%	6.6%	8.3%

RISK/RETURN PROFILE:



FUND MANAGERS:
Michael Moyle and David Knee

ASISA CATEGORY:
Global - Multi-Asset - Low Equity

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

INCEPTION DATE:
1 March 2004

FUND SIZE:
R107 918 876

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL HIGH YIELD BOND FUND OF FUNDS
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL INCOME

PERFORMANCE

The fund returned 0.9% in US dollar terms for the quarter, slightly behind its benchmark, the Barclays Capital Global Aggregate Bond Index, which returned 1.1%.

When translated into rand, the fund returned -8.0% relative to the benchmark of -7.8% as the rand strengthened by 8.8% over the quarter.

For the year, the fund earned 7.9% in US dollar terms, outperforming the benchmark by 0.5% whilst it returned 7.4%. As the rand gained 10.1% against the US dollar over the year, the resulting rand return for the fund is -3.0% compared to the benchmark return of - 3.5%.

For the quarter, the fund's exposure to emerging market local currency bonds via Mexico, Turkey and Brazil detracted from performance. This was largely offset by the fund's overweight position to credit, both European and US investment grade holdings.

MARKET OVERVIEW

The benign economic picture seen for much of the year continued in the fourth quarter of 2017. Global economic growth continued, as evidenced by data pointing to strong corporate earnings and trade output. This was supported by a low-inflation environment as policy-makers refrained from reducing stimulus. The US Federal Reserve continued its very gradual tightening, the Bank of England hiked interest rates for the first time in a decade, and the European Central Bank (ECB) kept interest rates unchanged. At quarter-end, the 10-year UST yield was trading around 2.4% from 2.3% at the end of Q3.

Global bonds delivered mixed returns with the US and German yield curves flattening, while credit, in particular investment grade outside of Europe, performed strongly.

The flattening of the US yield curve perhaps reflects a view that while the Federal Reserve will continue to tighten policy during 2018, the peak in US rates will be well below that of previous cycles since inflation remains well contained.

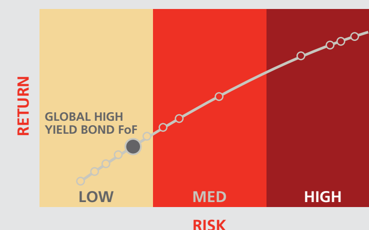
OUTLOOK

When considering valuations across asset classes in the context of the current economic environment, we continue to believe that mainstream government bond pricing remains distorted, and at these overvalued levels, these assets look vulnerable. However, we still see value in investment grade corporate bonds and some emerging market bonds on elevated levels of real yield.

Portfolio positioning remains unchanged and reflects the fund manager's preference for selected areas of credit (mainly US and European investment grade) based on the view that these assets are offering better value than mainstream government bonds at present. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	-3.0%	-3.5%
3 years	3.6%	4.2%
5 years	8.7%	8.6%
7 years	12.2%	11.4%
10 years	10.0%	9.4%
Since inception	8.2%	8.2%

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:
R353 521 228

AWARDS:
Raging Bull: 2006, 2008, 2013

Morningstar/Standard & Poor's: 2007, 2009, 2013

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL VALUE FUND OF FUNDS
31 DECEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL EQUITY

MARKET OVERVIEW

The final quarter of 2017 proved to be another strong one for global growth and stock markets, as numerous equity indices around the world in both developed and emerging economies rose to new records and posted double-digit returns for the year as a whole. The longstanding rally looked set to continue into the new year amid ongoing optimism over the health of the global economy, still-subdued inflation, supportive monetary policies and bullish investor sentiment, given an additional fillip by the enactment of major corporate tax cuts in the US. The US Federal Reserve continued its very gradual tightening, the Bank of England hiked interest rates for the first time in a decade, and the European Central Bank (ECB) kept interest rates unchanged.

PERFORMANCE

The fund returned 6.4% in US dollar terms for the quarter relative to the benchmark, the MSCI All Countries World Index, which returned 5.7%, an outperformance of 0.6%.

When translated into rand, the fund returned -3.0% relative to the benchmark of -3.6% as the rand strengthened by 8.8% over the quarter.

For the year, the fund earned 22.4% in US dollar terms whilst the benchmark returned 24.0%. As the rand gained 10.1% against the US dollar over the year, the resulting rand return for the fund is 10.0% compared to the benchmark return of 11.4%.

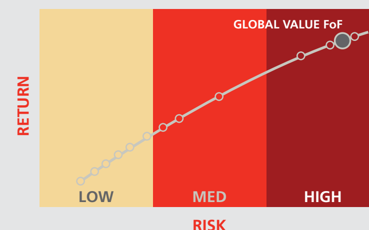
With relatively little dispersion of returns across markets for the quarter, the fund's allocation decisions contributed very little to relative returns.

STRATEGY AND OUTLOOK

The strong rallies in global equities seen over the past seven quarters in many countries has been driven in part by a re-rating of the MSCI All Country World Index, but strong corporate earnings growth has kept the Index within its fair value range. Investor sentiment remains somewhat pessimistic, although to a much lesser extent than 12 months ago. This presents opportunities to invest in cheaper markets, particularly in Europe, where there is considerable upside and where less optimism is already priced in as oppose to global indices and the broad US market. Furthermore our European positioning has been rebalanced towards small caps in order to benefit from a cyclical upswing and less efficient pricing. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	10.0%	11.4%
3 years	10.6%	11.6%
5 years	18.5%	19.4%
7 years	16.7%	18.8%
10 years	8.7%	11.0%
Since inception	6.8%	8.1%

RISK/RETURN PROFILE:



FUND MANAGERS:
David Knee and Michael Moyle

ASISA CATEGORY:
Global - Equity - General

BENCHMARK:
MSCI All Country World Index (Net)

INCEPTION DATE:
18 February 2000

FUND SIZE:
R271 143 134

DISCLAIMER

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Sources: Prudential, Morningstar & Deutsche Securities