PRUDENTIAL UNIT TRUSTS QUARTERLY COMMENTARY
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

COMBINED QUARTERLY COMMENTARY

Please **DOWNLOAD** this PDF pack to make use of the new interactive functionality

Click on the **"View commentary"** button to view the fact sheet of a specific fund.
Click the **"Home"** button to come back to this page.

INCOME FUNDS	
Money Market Fund	View commentary
High Interest Fund	View commentary
High Yield Bond Fund	View commentary
MULTI-ASSET FUNDS	
Enhanced Income Fund	View commentary
Inflation Plus Fund	View commentary
Balanced Fund	View commentary
PROPERTY/EQUITY FUNDS	
Enhanced SA Property Tracker Fund	View commentary
Dividend Maximiser Fund	View commentary
Equity Fund	View commentary
GLOBAL FUND OF FUNDS	
Global High Yield Bond Fund of Funds	View commentary
Global Cautious Managed Fund of Funds	View commentary
Global Value Fund of Funds	View commentary

HOW TO INVEST

0860 105 775
prudential.co.za
myprudential.co.za
query@myprudential.co.za

Application forms

Invest now

PRUDENTIAL MONEY MARKET FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

INCOME FUND

PERFORMANCE

Over the past quarter, the fund delivered a return of 1.9% (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 44 days relative to the 90-day maximum average duration.

MARKET OVERVIEW

A major local highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019).

Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

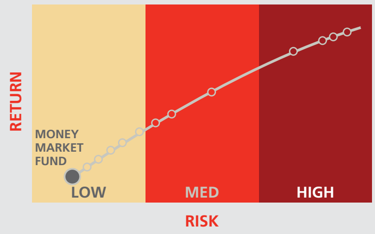
PPI inflation rose to 4.2% y/y in August from 3.6% y/y in July, mainly attributed to the fuel price component. Month-on-month, PPI came in at 0.4%.

Private sector credit extension (PSCE) rose to 6.0% y/y for August from 5.7% y/y in July. Corporates remain a driving factor, with growth in PSCE extended to corporates accelerating to 8.2% y/y from 7.8% previously. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	X CLASS
1 year	7.6%	6.9%	7.8%
3 years	6.9%	6.4%	7.0%
5 years	6.2%	5.8%	6.3%
7 years	6.0%	5.7%	n/a
10 years	7.1%	6.8%	n/a
Since inception	7.8%	7.7%	6.1%

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:
R3 128 275 152

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL HIGH INTEREST FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

INCOME FUND

PERFORMANCE

The Prudential High Interest Fund generated a return of 2.0% (net of fees) for the quarter, outperforming 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.

Relative to the 180-day maximum average duration, the quarter-end duration of the fund came in at 61 days.

MARKET OVERVIEW

South African equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand.

A major local highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019).

On another negative note, a reported R13 billion shortfall in government revenue collections sparked concerns National Treasury would miss its annual budget deficit target, not only raising the spectre of higher taxes in a weak environment, but also increasing the likelihood of further credit rating downgrades. Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

The improving inflation and interest rate outlook helped drive SA nominal bond prices higher (and yields lower) as the BEASSA All Bond Index returned 3.7% for the quarter, while inflation-linked bonds (Composite ILB Index) produced a more muted 1.4%. Cash as measured by the STeFI Composite Index returned 1.8% and SA listed property delivered 5.7%. The FTSE/JSE All Share Index reached record highs in August before retreating in September, still posting an impressive 8.9% return for the quarter. Gains were led by a 17.7% return from Resources shares on the back of stronger commodity prices, while Industrials produced 7.4% and Financials delivered a 5.1% return. The rand, meanwhile, weakened fairly sharply in September along with many other emerging market currencies: for the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient 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.

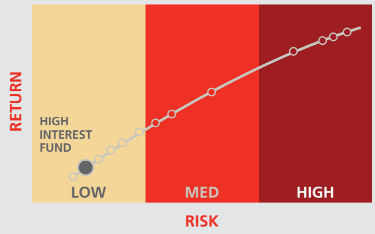
Exposure to floating-rate notes with 3-year terms was maintained over the quarter on the back of attractive pricing. While credit issuance has been scarce since 2016, mixed with a tightening of credit spreads, the quarter did see a number of banks and corporates coming to market, after some hesitance following the downgrade of the sovereign credit rating. Issuances were generally well supported and pricing was largely finalised towards the lower end or below the guided range.

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	8.4%	7.6%	8.6%	8.7%
2 years	8.0%	7.4%	8.2%	8.3%
3 years	7.4%	7.0%	7.6%	7.7%
5 years	6.7%	6.4%	6.8%	7.0%
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:
R10 092 875 778

PLEASE NOTE:
This fund is capped to new investors

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL HIGH YIELD BOND FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

PERFORMANCE

For the quarter, the fund returned 3.6% (net of fees), underperforming the benchmark, the BEASSA All Bond Index, which returned 3.7%. It outperformed cash (as measured by the STeFI Composite Index), which returned 1.8%, and inflation-linked bonds at 1.4% (JSE CILI). We retained our neutral duration position over the quarter. 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, Q2 GDP growth was revised significantly upward to 3.0% (q/q annualised) from its previous 2.6% estimate, on the back of higher household spending and business investment. At the same time, September saw: 1) a rise in US August CPI to 1.9% y/y (above expectations and closer to the Federal Reserve Bank's 2.0% target); 2) a clearly more hawkish tone from the Fed; and 3) speculation around the appointment of a more hawkish Fed Chairman to replace Janet Yellen – Kevin Warsh, a former Fed governor. These were among the primary reasons investors moved forward their expectations for the next 25bp interest rate hike to December.

At its September FOMC meeting, the Fed discounted damage to the economy from hurricanes Harvey, Irma and Maria as being of a short-term and relatively localized nature. Yellen's comments that it would be "imprudent" to keep monetary policy on hold until inflation reached the 2.0% target were widely interpreted as signalling another rate hike in December – 25bps was nearly fully priced in to the market. Yellen also announced details of the Fed's plans to unwind its $4.5 balance sheet of securities accumulated during quantitative easing (QE), starting from October. However, the central bank still forecasts only three 25bp rate hikes in 2018, expecting ongoing steady growth and low unemployment to push inflation higher.

In the Eurozone, the region's growth accelerated to 2.1% (q/q annualised) in Q2 from Q1's 1.9%, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. CPI at 1.5% in August was also higher than expected, due mainly to rising energy prices, while growth forecasts were revised further upward and the euro appreciated against the US dollar. At its September meeting the ECB left interest rates on hold, while paving the way for a tapering of its quantitative easing programme.

The UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment. The weaker pound over the quarter continued to drive up the cost of imports and inflation: August CPI accelerated to 2.9% y/y, above the 2.8% expected. At its September policy meeting, the Bank of England said its concerns over inflation now outweighed those over Brexit-related risks to the economy, although it left its base interest rate unchanged. Investors now see the chances of an interest rate hike before year-end as much higher.

In Japan, Q2 GDP growth jumped to 4.0% (q/q annualised), far exceeding the 2.5% expected thanks to strong household consumption and business investment during the quarter. This marked six successive quarters of growth, the longest streak since 2006. However, inflation remained subdued at only 0.9% y/y in August, and excluding energy and food costs was flat.

In China, Q2 GDP growth surprised to the upside at 6.9% (q/q annualised), unchanged from Q1 and above 2017's official 6.5% growth target, with factory output boosted by improving global trade and higher domestic demand. Following Moody's downgrade in May, S&P downgraded the country's credit rating one notch to A+ from AA-, citing the "soaring debt burden".

In South Africa Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA.

Further, a reported R13 billion shortfall in government revenue collections sparked concerns National Treasury would miss its annual budget deficit target, not only raising the spectre of higher taxes in a weak environment, but also increasing the likelihood of further credit rating downgrades. Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

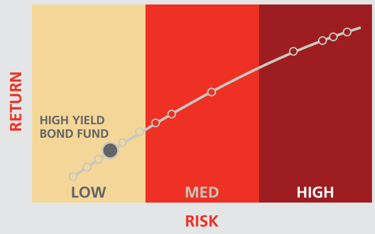
SA nominal bond yields fell over the quarter although September did see a partial retracement of this rally. We continue to prefer longer-dated government bonds due to the more attractive yields on offer and are comfortable with the compensation provided for the extra risk involved. ■

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

INCOME FUND

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:
R532 030 120

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL ENHANCED INCOME FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

PERFORMANCE

For the three months ending 30 September 2017, the fund returned 2.8% (net of fees) beating its benchmark as measured by the STeFi composite by 1.0%. The top contributors to performance were holdings of SA cash, SA nominal bonds (both corporate and government) and SA listed property. The fund's international exposure also contributed positively. For the 12-month period, the fund has delivered 8.1% (net of fees), outperforming its benchmark by 0.5%.

MARKET OVERVIEW

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar (until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

While growth prospects remained buoyant, data showing higher-than-expected August inflation across the US, UK and Eurozone prompted more hawkish comments from the respective central banks. This, in turn, led investors to expect interest rate tightening earlier than previously anticipated. While this sent developed market equities and currencies higher in September, it sparked sales of US and European bonds, as well as emerging market equities and currencies. In September, South African equities, bonds and the rand all pared their earlier quarterly gains.

In the US, Q2 GDP growth was revised significantly upward to 3.0% (q/q annualised) from its previous 2.6% estimate, on the back of higher household spending and business investment. At the same time, September saw: 1) a rise in US August CPI to 1.9% y/y (above expectations and closer to the Federal Reserve Bank's 2.0% target); 2) a clearly more hawkish tone from the Fed; and 3) speculation around the appointment of a more hawkish Fed Chairman to replace Janet Yellen – Kevin Warsh, a former Fed governor. These were among the primary reasons investors moved forward their expectations for the next 25bp interest rate hike to December. With rates anticipated to move higher sooner, US equities and the dollar became more attractive, prompting a move away from emerging market equities in particular at the end of the quarter.

At its September FOMC meeting, the Fed discounted damage to the economy from hurricanes Harvey, Irma and Maria as being of a short-term and relatively localized nature. Yellen's comments that it would be "imprudent" to keep monetary policy on hold until inflation reached the 2.0% target were widely interpreted as signaling another rate hike in December – 25bps was nearly fully priced in to the market. Yellen also announced details of the Fed's plans to unwind its $4.5 trillion balance sheet of securities accumulated during quantitative easing (QE), starting from October. However, the central bank still forecasts only three 25bp rate hikes in 2018, expecting ongoing steady growth and low unemployment to push inflation higher. US bond yields rose as a result of the Fed's somewhat more aggressive stance. At the same time, equities were supported, and US bonds hurt, by growing optimism over a growth boost from likely tax cuts under the Republican administration.

The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, returned 1.8% in the quarter. While US bonds were stronger for much of the period, they erased all of their gains in September as the likelihood of an earlier interest rate hike rose and data confirmed growing inflationary pressures. At quarter-end the 10-year UST yield was barely changed at 2.33% from 2.31% at the end of Q2. For US corporate bonds, investment-grade bond spreads narrowed slightly to 106bps over USTs, while high-yield spreads also narrowed somewhat.

In the Eurozone, the region's growth accelerated to 2.1% (q/q annualised) in Q2 from Q1's 1.9%, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. CPI at 1.5% in August was also higher than expected, due mainly to rising energy prices, while growth forecasts were revised further upward and the euro appreciated against the US dollar – the currency is 13% stronger against the greenback so far in 2017. Manufacturing PMI data for September in both France and Germany came in at the highest levels in six years. At its September meeting the ECB left interest rates on hold, while paving the way for a tapering of its quantitative easing programme.

Meanwhile, the UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment. The weaker pound over the quarter continued to drive up the cost of imports and inflation: August CPI accelerated to 2.9% y/y, above the 2.8% expected. At its September policy meeting, the Bank of England said its concerns over inflation now outweighed those over Brexit-related risks to the economy, although it left its base interest rate unchanged. Investors now see the chances of an interest rate hike before year-end as much higher.

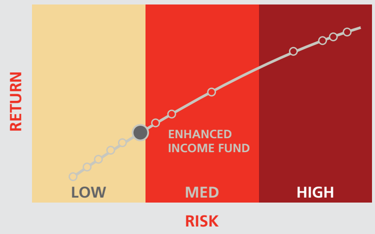
In China, Q2 GDP growth surprised to the upside at 6.9% (q/q annualised), unchanged from Q1 and above 2017's official 6.5% growth target, with factory output boosted by improving global trade and higher domestic demand. The upcoming Communist party conference in October meant government and the central bank were focused on maintaining financial market stability, underpinning asset strength for the quarter. The equity market continued its remarkable performance with the MSCI China returning 14.8% in Q3: it has now delivered 43.4% for the year to 30 September. Notably, following Moody's downgrade in May, S&P downgraded the country's credit rating one notch to A+ from AA-, citing the "soaring debt burden". Although September manufacturing PMI rose to 52.4 from 51.7 in August, its fastest since 2012, analysts expect a small slowdown in GDP growth in the third quarter of 2017.

In South Africa, equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand.

A major SA highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019).

On another negative note, a reported R13 billion shortfall in government revenue collections sparked concerns National Treasury would miss its annual budget deficit target, not only raising the spectre of higher taxes in a weak environment, but also increasing the likelihood of further credit rating downgrades. Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in

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 387 462 472

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	X CLASS	D CLASS
1 year	8.1%	7.6%	8.6%	8.3%	8.7%
3 years	7.8%	7.5%	n/a	8.1%	8.5%
5 years	7.4%	6.4%	n/a	7.6%	8.0%
7 years	8.0%	7.1%	n/a	n/a	n/a
Since inception	8.7%	7.3%	7.8%	8.4%	8.7%

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

Sources: Prudential, Morningstar & Deutsche Securities

September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

The improving inflation and interest rate outlook helped drive SA nominal bond prices higher (and yields lower) as the BEASSA All Bond Index returned 3.7% for the quarter, while inflation-linked bonds (Composite ILB Index) produced a more muted 1.4%. Cash as measured by the STeFI Composite Index returned 1.8% and SA listed property delivered 5.7%. The rand, meanwhile, weakened fairly sharply in September along with many other emerging market currencies: for the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro.

STRATEGY AND OUTLOOK

SA listed property fundamentals have deteriorated somewhat in the recent period. Although benefitting from the improved inflation and interest rate outlook, deteriorating medium-term economic growth prospects in South Africa 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 with a forward distribution yield of 7.4% at quarter-end.

Exposure to SA nominal bonds is broadly unchanged, despite the fall in yields over the quarter (although September saw a partial retracement of this drop). We continue to prefer longer-dated government bonds due to the more attractive yields on offer. We are comfortable with the compensation provided for the extra risk involved.

Inflation-linked bonds saw their valuation fall to attractive levels relative to nominal bonds over the quarter (amid the improved inflation outlook). We took advantage of this and bought more ILBs. 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. ■

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL INFLATION PLUS FUND
30 SEPTEMBER 2017

PRUDENTIAL INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

MARKET OVERVIEW

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar (until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

While growth prospects remained buoyant, data showing higher-than-expected August inflation across the US, UK and Eurozone prompted more hawkish comments from the respective central banks. This, in turn, led investors to expect interest rate tightening earlier than previously anticipated. While this sent developed market equities and currencies higher in September, it sparked sales of US and European bonds, as well as emerging market equities and currencies. In September, South African equities, bonds and the rand all pared their earlier quarterly gains.

US stock markets again reached fresh record highs, but worries mounted over high valuations, with swings in sentiment towards tech stocks in particular. For Q3, the S&P 500 returned 4.5% and the Nasdaq 6.2% (but -0.1% in September). The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, returned 1.8% in the quarter. While US bonds were stronger for much of the period, they erased all of their gains in September. At quarter-end the 10-year UST yield was barely changed at 2.33% from 2.31% at the end of Q2. For US corporate bonds, both investment-grade and high-yield bond spreads narrowed slightly.

In the Eurozone, growth accelerated in Q2, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. At its September meeting the ECB left interest rates on hold, while paving the way for a tapering of its quantitative easing programme. For the quarter, the Dow Jones Eurostoxx 50 returned 8.5%, while Germany's DAX 30 delivered 7.6% and the French CAC 40 7.8% (all in US$). Meanwhile, the UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment. The weaker pound continued to drive up inflation: At its September policy meeting, the Bank of England said its concerns over inflation now outweighed those over Brexit-related risks to the economy, although it left its base interest rate unchanged. Investors now see the chances of an interest rate hike before year-end as much higher. The FTSE 100 returned 4.8% (in US$) over the quarter.

In Japan, Q2 GDP growth jumped to 4.0% (q/q annualised), far exceeding the 2.5% expected thanks to strong household consumption and business investment during the quarter. This marked six successive quarters of growth, the longest streak since 2006. The Nikkei 225 Index returned 2.1% over the quarter (in US$). In China, Q2 GDP growth surprised to the upside at 6.9% (q/q annualised), with factory output boosted by improving global trade and higher domestic demand. The upcoming Communist party conference in October meant government and the central bank were focused on maintaining financial market stability, underpinning asset strength for the quarter. The equity market continued its remarkable performance with the MSCI China returning 14.8% in Q3.

Other emerging market (EM) assets posted strong returns in Q3 as risk-hungry investors continued to seek out EM equities and bonds, although in September demand waned. Overall, the MSCI Emerging Markets Index returned 8.0% in US$ (but -0.4% in September). This compared to 5.0% from the MSCI World Index for developed markets.

South African equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand.

A major local highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019).

Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

The improving inflation and interest rate outlook helped drive SA nominal bond prices higher (and yields lower) as the BEASSA All Bond Index returned 3.7% for the quarter, while inflation-linked bonds (Composite ILB Index) produced a more muted 1.4%. Cash as measured by the STeFI Composite Index returned 1.8% and SA listed property delivered 5.7%. The FTSE/JSE All Share Index reached record highs in August before retreating in September, still posting an impressive 8.9% return for the quarter. Gains were led by a 17.7% return from Resources shares on the back of stronger commodity prices, while Industrials produced 7.4% and Financials delivered a 5.1% return. The rand, meanwhile, weakened fairly sharply in September along with many other emerging market currencies: for the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro.

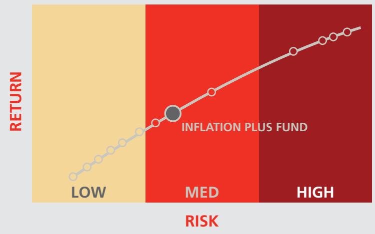
PERFORMANCE

The fund returned 4.6% (after fees) for the third quarter of 2017 and has returned 5.9% for the 12-month period ending 30 September 2017. The fund has delivered a return of 13.0% per annum since inception (after fees), compared to its after-fee objective of 9.6% per annum over the same period. To 30 September 2017 it retains

ANNUALISED PERFORMANCE	A CLASS	OBJECTIVE#	T CLASS	X CLASS	B CLASS
1 year	5.9%	8.1%	6.4%	6.1%	6.7%
3 years	7.4%	8.5%	n/a	7.7%	8.2%
5 years	10.2%	9.0%	n/a	10.5%	11.0%
7 years	11.2%	8.9%	n/a	n/a	12.0%
10 years	9.9%	9.6%	n/a	n/a	10.7%
Since inception	13.0%	9.6%	6.6%	11.9%	12.9%

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 class -0.9%.

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 248 467 407

AWARDS:
Raging Bull: 2013
Morningstar: 2015

Sources: Prudential, Morningstar & Deutsche Securities

its top-quartile or better performance over annual periods from 4-10 years, according to Morningstar. The largest contributors to returns for the quarter were the fund's holdings in SA equities, followed by international equities. Within this, exposure to Japan, the US and Europe added value, while Turkish equities detracted modestly. Other contributors included, to a lesser extent, SA listed property, SA bond and SA ILB exposure, followed by SA cash. The fund's holdings in large global stocks like Naspers and BAT were significant contributors to performance for the quarter, while its selection of financial shares including Standard Bank, First Rand and Old Mutual also added value (to a lesser extent). The fund's holdings of SA corporate bonds also contributed positively to returns.

STRATEGY AND OUTLOOK

In **global fixed income**, despite recent rises in government bond yields, they continue to trade at very low levels historically. They remain at risk to rising interest rates in the US and and increasingly in Europe and the UK as well. We continue to be underweight global sovereign bonds and underweight duration to reduce interest rate risk. After having used our global cash holdings to buy more investment-grade US and European corporate bonds in the previous quarter, we are now underweight foreign cash, and overweight foreign corporate bonds. We hold little high yield corporate bond exposure.

For **global equities**, despite good price gains over the past six quarters and record stock market highs in some countries, the MSCI All Country World Index remains within its "fair value" range with a 12-month forward P/E ratio of 16X at the end of September from 15.8X at the beginning of the quarter – this due to strong corporate earnings growth over the period. Against the backdrop of broad global growth, we see better value in many regions compared to South Africa, which is why we prefer global equity to South African equity in the fund, given its 40% equity exposure limit. Our current equity positioning reflects a preference for cheaper areas where fundamentals remain encouraging: the fund's top overweight markets comprise South Korea, Turkey and the UK, and top underweights are the US, Canada and France, given their relative high valuations.

In South Korea, for example, after five years of disappointing corporate earnings growth (and downgraded expectations), earnings growth has been surprising to the upside over the past 12 months: while the KOSPI has returned 20.4% in US dollars in the past year, its 12-month forward P/E ratio has fallen from 10.2X to 9.5X to end-September thanks to rapid earnings growth. Growth contributors include large tech conglomerates like Samsung which are participating in the global "tech wave" that has sent the US Nasdaq index to record highs.

South African equities became more expensive in Q3, with the FTSE/JSE ALSI 12-month forward P/E rising to 14.6X at quarter-end from around 14X in Q2. Although local equities are still attractively priced in their "fair value" range, we see better opportunities offshore in the context of the Inflation Plus Fund's 40% total equity exposure limit. Consequently we moved slightly underweight SA equity in the Prudential Inflation Plus Fund during the quarter.

Prudential's equity holdings are similar to the previous quarter. Our portfolios are overweight stocks with solid foreign currency earnings like British American Tobacco, Capital & Counties, Anglo American and Exxaro, as well as international container transport group Trencor, which has upside to improving global trade trends. We also hold non-mining resources stocks like Sappi. We remain overweight in well-priced and high-yielding Financials including Old Mutual, Investec, Standard Bank and Barclays Group Africa. We have maintained our underweight in Retail stocks given the challenging consumer environment, but do continue to hold selective overweights in Foschini and Pick 'n Pay. We have preferred to gain our consumer exposure via well-priced and more defensive consumer services providers like Sun International.

In **SA listed property**, we pared our holdings to a neutral position from overweight, as fundamentals for the sector have deteriorated somewhat in the recent period. Although benefitting from the improved inflation and interest rate outlook, deteriorating medium-term economic growth prospects in South Africa 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 with a forward distribution yield of 7.4% at quarter-end.

In **SA nominal bonds**, we remain overweight despite the fall in yields over the quarter (although September saw a partial retracement of this drop). We continue to prefer longer-dated government bonds due to the more attractive yields on offer. We are comfortable with the compensation provided for the extra risk involved.

Inflation-linked bonds saw their valuation fall to attractive levels relative to nominal bonds over the quarter (amid the improved inflation outlook). We took advantage of this to buy more ILBs, moving from an underweight position in our multi-asset portfolios to a neutral position. ■

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL BALANCED FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

MULTI-ASSET

PERFORMANCE

The fund enjoyed a strong quarter, gaining 5.4% (net of fees in rand) compared to the 5.1% returned by its benchmark. All asset classes enjoyed positive gains, with the main contributors being the strong returns from equities – both domestic and international – over the quarter. The fund's holdings of SA cash, nominal bonds and listed property all contributed as well.

In terms of its international exposure, the bullish global environment worked well for the portfolio's positioning in favour of risk assets. The main contributors to performance were its exposures to the core MSCI World Index and the S&P 500 Index. Other equity contributions came from its Japanese equity and emerging markets equity exposure, although exposures to emerging Asia detracted slightly. The portfolio's global fixed income holdings added modestly to value, in particular its exposure to emerging market bonds and US investment grade bonds. The portfolio's small global property holding also contributed.

Over the past 12 months, the fund has returned 8.3%, outperforming the benchmark's 6.0% total return, while over the past five years it has delivered a 12.3% total return versus 9.8% from the benchmark.

MARKET OVERVIEW

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar (until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

While growth prospects remained buoyant, data showing higher-than-expected August inflation across the US, UK and Eurozone prompted more hawkish comments from the respective central banks. This, in turn, led investors to expect interest rate tightening earlier than previously anticipated. While this sent developed market equities and currencies higher in September, it sparked sales of US and European bonds, as well as emerging market equities and currencies. South African assets saw some of their good quarterly gains pared in September.

In the US, Q2 GDP growth was revised significantly upward to 3.0% (q/q annualised) from its previous 2.6% estimate, on the back of higher household spending and business investment. At the same time, September saw: 1) a rise in US August CPI to 1.9% y/y (above expectations and closer to the Federal Reserve Bank's 2.0% target); 2) a clearly more hawkish tone from the Fed; and 3) speculation around the appointment of a more hawkish Fed Chairman to replace Janet Yellen – Kevin Warsh, a former Fed governor. These were among the primary reasons investors moved forward their expectations for the next 25bp interest rate hike to December. With rates anticipated to move higher sooner, US equities and the dollar became more attractive, prompting a move away from emerging market equities in particular at the end of the quarter.

At its September FOMC meeting, the Fed discounted damage to the economy from hurricanes Harvey, Irma and Maria as being of a short-term and relatively localized nature. Yellen's comments that it would be "imprudent" to keep monetary policy on hold until inflation reached the 2.0% target were widely interpreted as signalling another rate hike in December – 25bps was nearly fully priced in to the market. Yellen also announced details of the Fed's plans to unwind its $4.5 trillion balance sheet of securities accumulated during quantitative easing (QE), starting from October. However, the central bank still forecasts only three 25bp rate hikes in 2018, expecting ongoing steady growth and low unemployment to push inflation higher. US bond yields rose as a result of the Fed's somewhat more aggressive stance. At the same time, equities were supported, and US bonds hurt, by growing optimism over a growth boost from likely tax cuts under the Republican administration.

US stock markets again reached fresh record highs, but worries mounted over high valuations, with swings in sentiment towards tech stocks in particular. For Q3, the S&P 500 returned 4.5% and the Nasdaq 6.2% (but -0.1% in September). The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, returned 1.8% in the quarter. While US bonds were stronger for much of the period, they erased all of their gains in September as the likelihood of an earlier interest rate hike rose and data confirmed growing inflationary pressures. At quarter-end the 10-year UST yield was barely changed at 2.33% from 2.31% at the end of Q2. For US corporate bonds, investment-grade bond spreads narrowed slightly to 106bps over USTs, while high-yield spreads also narrowed somewhat.

In the Eurozone, the region's growth accelerated to 2.1% (q/q annualised) in Q2 from Q1's 1.9%, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. CPI at 1.5% in August was also higher than expected, due mainly to rising energy prices, while growth forecasts were revised further upward and the euro appreciated against the US dollar – the currency is 13% stronger against the greenback so far in 2017. Manufacturing PMI data for September in both France and Germany came in at the highest levels in six years. At its September meeting the ECB left interest rates on hold, while paving the way for a tapering of its quantitative easing programme. For the quarter, the Dow Jones Eurostoxx 50 returned 8.5%, while Germany's DAX 30 delivered 7.6% and the French CAC 40 7.8% (all in US$).

Meanwhile, the UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment. The weaker pound over the quarter continued to drive up the cost of imports and inflation: August CPI accelerated to 2.9% y/y, above the 2.8% expected. At its September policy meeting, the Bank of England said its concerns over inflation now outweighed those over Brexit-related risks to the economy, although it left its base interest rate unchanged. Investors now see the chances of an interest rate hike before year-end as much higher. The FTSE 100 returned 4.8% (in US$) over the quarter.

In Japan, Q2 GDP growth jumped to 4.0% (q/q annualised), far exceeding the 2.5% expected thanks to strong household consumption and business investment during the quarter. This marked six successive quarters of growth, the longest streak since 2006. However, inflation remained subdued at only 0.9% y/y in August, and excluding energy and food costs was flat. Investors are questioning the Bank of Japan's and Prime Minister Abe's aggressive four-year-long reflationary efforts, with growing calls to abandon the inflation target. Abe has called for an election on 22 October, which he is expected to win despite growing unpopularity. The Nikkei 225 Index returned 2.1% over the quarter (in US$).

In China, Q2 GDP growth surprised to the upside at 6.9% (q/q annualised), unchanged from Q1 and above 2017's official 6.5% growth target, with factory output boosted by improving global trade and higher domestic demand. The upcoming Communist party conference in October meant government and the central bank were focused on maintaining financial market stability, underpinning asset strength for the quarter. The equity market continued its remarkable performance with the MSCI China returning 14.8% in Q3: it has now delivered 43.4% for the year to 30 September. Notably, following Moody's downgrade in May, S&P downgraded the country's credit rating one notch to A+ from AA-, citing the "soaring debt burden". Although September manufacturing PMI rose to 52.4 from 51.7 in August, its fastest since 2012, analysts expect a small slowdown in GDP growth in the third quarter of 2017.

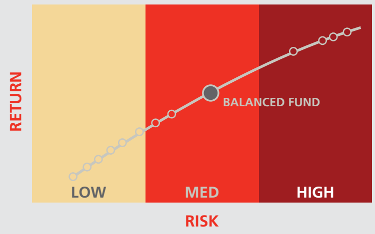
Other emerging market (EM) assets posted strong returns in Q3 as risk-hungry investors continued to seek out EM equities and bonds, although in September equity demand waned. Overall, the MSCI Emerging Markets Index returned 8.0% in US$ (but -0.4% in September). This compared to 5.0% from the MSCI World Index for developed markets. Among the larger EM equity markets in US$ terms for the quarter, Brazil's Bovespa was the strongest performer with a 23.3% total return, followed by the MSCI Russia (18.1%) and the MSCI China (14.8%). The poorest Q3 returns (in US$) came from the MSCI Turkey (0.4%) and the MSCI India (3.0%). The MSCI South Africa (in US$) produced 4.0%, for a 12.7% return year to date.

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	X CLASS	B CLASS
1 year	8.3%	6.0%	8.9%	8.5%	9.1%
3 years	7.9%	6.3%	n/a	8.1%	8.7%
5 years	12.3%	9.8%	n/a	n/a	13.2%
7 years	12.4%	9.9%	n/a	n/a	13.3%
10 years	10.0%	8.1%	n/a	n/a	10.9%
Since inception	14.4%	12.3%	6.9%	11.2%	14.7%

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

ASSET CLASS RETURNS	Q2 2017	YTD
SA Equity (FTSE/JSE All Share Index)	-0.4%	3.4%
SA Property (FTSE/JSE SA Listed property Index)	0.9%	2.3%
SA Bonds (BEASSA All Bond Index)	1.5%	4.0%
SA Inflation-linked Bonds (RSA Composite Inflation-linked Bond Index)	1.0%	0.4%
SA Cash (STeFI Composite)	1.9%	3.7%
Global Equity (MSCI World Index - USD)	4.0%	10.7%
Global Equity (MSCI Emerging Markets Index – USD)	6.3%	18.4%
Global Bonds (Barclays Global Aggregate Bond Index – USD)	2.6%	14.4%
Rand (Rand/USD move)	-2.3%	-4.4%

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:

R17 054 187 407

Sources: Prudential, Morningstar & Deutsche Securities

QUARTERLY COMMENTARY

In commodities, the price of Brent crude surged some 20.1% during the quarter to around $56.70 per barrel at quarter end, driven by mounting signs that the three-year market oversupply is finally easing on the back of production cuts by OPEC and other producers. Other commodity prices also moved higher in line with accelerating global growth and a weaker dollar towards the end of the period. Gold gained 3.1% largely on the back of North Korean tensions, and palladium rose 11.2%. Platinum, however, lost 1.5% on oversupply concerns. Among industrial metals, the bellwether copper gained 8.5%, zinc was up 16.4%, nickel increased 11.4%, lead rose 9.6% and aluminium was 8.7% higher.

SA returns lifted by bullish global growth sentiment

South African equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand.

A major local highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019).

On another negative note, a reported R13 billion shortfall in government revenue collections sparked concerns National Treasury would miss its annual budget deficit target, not only raising the spectre of higher taxes in a weak environment, but also increasing the likelihood of further credit rating downgrades. Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

The improving inflation and interest rate outlook helped drive SA nominal bond prices higher (and yields lower) as the BEASSA All Bond Index returned 3.7% for the quarter, while inflation-linked bonds (Composite ILB Index) produced a more muted 1.4%. Cash as measured by the STeFI Composite Index returned 1.8% and SA listed property delivered 5.7%. The FTSE/JSE All Share Index reached record highs in August before retreating in September, still posting an impressive 8.9% return for the quarter. Gains were led by a 17.7% return from Resources shares on the back of stronger commodity prices, while Industrials produced 7.4% and Financials delivered a 5.1% return. The rand, meanwhile, weakened fairly sharply in September along with many other emerging market currencies: for the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro.

STRATEGY AND OUTLOOK

For our general offshore exposure, the Prudential Balanced Fund continues to be very near our maximum permitted 25% offshore weighting, and is overweight global equities while being underweight global bonds and cash. The large equity risk premium remains the most obvious opportunity on offer today, in our view.

In **global fixed income**, despite recent rises in government bond yields, they continue to trade at very low levels historically. They remain at risk to rising interest rates in the US and UK, and increasingly in Europe as well, particularly should we see higher-than-expected inflation as we did in September. We continue to be underweight global sovereign bonds and underweight duration to reduce interest rate risk. After having used our global cash holdings to buy more investment-grade US and European corporate bonds in the previous quarter, we are now underweight foreign cash, and overweight foreign corporate bonds. We hold little high yield corporate exposure.

For **global equities,** despite good price gains over the past six quarters and record stock market highs in some countries, the MSCI All Country World Index remains within its "fair value" range with a 12-month forward P/E ratio of 16X at the end of September from 15.8X at the beginning of the quarter – this due to strong corporate earnings growth over the period. Against the backdrop of broad global growth, we see better value in many regions compared to South Africa, which is why we prefer global equity to South African equity. Our current equity positioning reflects a preference for cheaper areas where fundamentals remain encouraging including Europe, Japan, the global financial sector and smaller holdings in selected emerging markets such as Korea, Turkey and Indonesia, compared to global indices and the broad US market.

In South Korea, for example, after five years of disappointing corporate earnings growth (and downgraded expectations), earnings growth has been surprising to the upside over the past 12 months: while the KOSPI has returned 20.4% in US dollars in the past year, its 12-month forward P/E ratio has fallen from 10.2X to 9.5X to end September thanks to rapid earnings growth. Growth contributors include large tech conglomerates like Samsung which are participating in the global "tech wave" that has sent the US Nasdaq index to record highs.

South African equities became more expensive in Q3, with the FTSE/JSE ALSI 12-month forward P/E rising to 14.6X at quarter-end from around 14X in Q2. Despite this, local equities are still priced in their "fair value" range, and the fund held a broadly neutral position in this asset class over the quarter compared to the benchmark.

Prudential's equity holdings are similar to the previous quarter. The fund holds stocks with solid foreign currency earnings like British American Tobacco, Richemont and Naspers, with the latter contributing notably to returns over the quarter. Resources stocks like Anglo American, BHP Billiton and Exxaro, also added significant value. We also hold non-mining resources stocks like Sappi. We remain overweight in well-priced and high-yielding Financials including Old Mutual, Investec, Standard Bank and FirstRand. We have maintained our underweight in Retail stocks given the challenging consumer environment, but do continue to hold selective overweights in Foschini and Pick 'n Pay.

In **SA listed property**, we pared our overweight holdings during the quarter, but the fund remains somewhat overweight in this asset class. Fundamentals for the sector have deteriorated somewhat in the recent period, although it is benefitting from the improved inflation and interest rate outlook. Listed property is trading around its fair value with a forward distribution yield of 7.4% at quarter-end.

In **SA nominal bonds**, we remain overweight despite the fall in yields over the quarter (although September saw a partial retracement of this drop). We continue to prefer longer-dated government bonds due to the more attractive yields on offer. We are comfortable with the compensation provided for the extra risk involved.

Inflation-linked bonds saw their valuation fall to attractive levels relative to nominal bonds over the quarter (amid the improved inflation outlook). We took advantage of this to buy more ILBs, moving from an underweight position in our multi-asset portfolios to a neutral position. ■

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL ENHANCED SA PROPERTY TRACKER FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

PROPERTY

PERFORMANCE

The fund recorded a return of 5.4% (net of fees) for the quarter compared to its benchmark, the SA Listed Property (SAPY) index, which returned 5.7%. Over the past year the fund returned 9.2%, underperforming the benchmark by 0.3%. The fund's underperformance over this period can be attributed to management fees offset by active stock selection of our fundamental strategy of holding excess weight in higher-yielding stocks. The 10-year track record of the fund ranks it third out of its peers, with the fund having outperformed the benchmark (after fees) over this period.

MARKET COMMENTARY

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar (until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

US stock markets again reached fresh record highs, but worries mounted over high valuations, with swings in sentiment towards tech stocks in particular. For Q3, the S&P 500 returned 4.5% and the Nasdaq 6.2% (but -0.1% in September). The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, returned 1.8% in the quarter.

In the Eurozone, the region's growth accelerated to 2.1% (q/q annualised) in Q2 from Q1's 1.9%, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. CPI at 1.5% in August was also higher than expected, due mainly to rising energy prices, while growth forecasts were revised further upward and the euro appreciated against the US dollar – the currency is 13% stronger against the greenback so far in 2017. Meanwhile, the UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment.

South African equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand. On a negative note, a reported R13 billion shortfall in government revenue collections sparked concerns National Treasury would miss its annual budget deficit target, not only raising the spectre of higher taxes in a weak environment, but also increasing the likelihood of further credit rating downgrades. Meanwhile, although the SARB enacted a surprise 25bp rate cut in July – its first in five years – in September it left rates on hold; this despite August CPI coming in at 4.8% y/y, slightly higher than the 4.6% y/y recorded in July (on the back of higher energy prices) but within the SARB's 4-6% target range. The SARB cited growing upside risks to inflation arising from the weaker rand (in September), policy uncertainty, growing fiscal challenges and more possible downgrades.

The improving inflation and interest rate outlook helped drive SA nominal bond prices higher (and yields lower) as the BEASSA All Bond Index returned 3.7% for the quarter, while inflation-linked bonds (Composite ILB Index) produced a more muted 1.4%. Cash as measured by the STeFI Composite Index returned 1.8% and SA listed property delivered 5.7%.

In the SA listed property sector, actual delivered growth in distributions per share for the major listed property companies averaged 13.3% for the quarter, lifted by NEPI, Fortress and Mas.

The recent results from SA-focussed REITs for periods ending 30 September have been broadly in line with expectations for growth below historic levels, while the offshore counters have delivered positive surprises driven by sound property fundamentals and earnings-enhancing M&A activity. One exception to this was the negative earnings surprise from Accelerate Property Fund which, due to acquisitions that are earnings-dilutive as well as dilutive funding required for corporate activity, guided the market to flat distribution growth for the next two years.

During the quarter, two international counters, NEPI and Rockcastle merged, with the new company becoming the largest REIT listed on the JSE. They subsequently undertook their first capital raise as a merged entity and raised R5.2bn. Greenbay, another international property stock, has recently been included in the SAPY and has raised R7.7bn this year so far, while Mas Real Estate Fund has raised R2bn in the last quarter alone. All of this indicates that there is currently more appetite for opportunities offshore.

Trading densities in South Africa have come increasingly under pressure as the year has progressed. During the last quarter Stuttafords, which entered business rescue in October 2016, ceased operation 1 August. The property counters in the sector most adversely affected by Stuttafords store closures are Hyprop and Liberty 2 Degrees. Edcon remains a material risk to vacancies in the sector.

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.

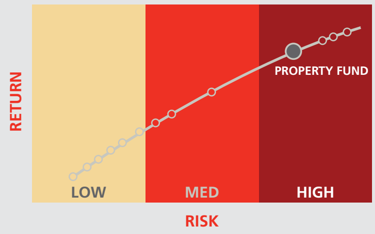
In the absence of a material de-rating in the market's valuation, listed property is priced to comfortably deliver double-digit returns over the medium term, well above inflation.

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	9.2%	9.5%	9.3%	9.4%
3 years	13.4%	12.7%	n/a	13.6%
5 years	13.2%	12.7%	n/a	13.3%
7 years	15.3%	15.2%	n/a	15.5%
10 years	14.1%	13.9%	n/a	n/a
Since inception	16.4%	16.5%	6.2%	16.9%

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

RISK/RETURN PROFILE:



FUND MANAGERS:
Duncan Schwulst

ASISA CATEGORY:
South African - Real Estate - General

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

INCEPTION DATE:
2 December 2005

FUND SIZE:
R7 817 953 462

AWARDS:
Morningstar/Standard & Poor's: 2011

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL DIVIDEND MAXIMISER FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

PERFORMANCE

The fund returned 6.7% (net of fees) for the three months ended 30 September 2017, outperforming its benchmark which returned 6.0%. For the past 12 months the fund has outperformed by a full 5.0%, with a return of 9.2% (net of fees) versus 4.2% from the benchmark.

MARKET OVERVIEW

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar (until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

While growth prospects remained buoyant, data showing higher-than-expected August inflation across the US, UK and Eurozone prompted more hawkish comments from the respective central banks. This, in turn, led investors to expect interest rate tightening earlier than previously anticipated. While this sent developed market equities and currencies higher in September, it sparked sales of US and European bonds, as well as emerging market equities and currencies. In September, South African equities, bonds and the rand all pared their earlier quarterly gains.

In the US, Q2 GDP growth was revised significantly upward to 3.0% (q/q annualised) from its previous 2.6% estimate, on the back of higher household spending and business investment. At the same time, September saw: 1) a rise in US August CPI to 1.9% y/y (above expectations and closer to the Federal Reserve Bank's 2.0% target); 2) a clearly more hawkish tone from the Fed; and 3) speculation around the appointment of a more hawkish Fed Chairman to replace Janet Yellen – Kevin Warsh, a former Fed governor. These were among the primary reasons investors moved forward their expectations for the next 25bp interest rate hike to December. With rates anticipated to move higher sooner, US equities and the dollar became more attractive, prompting a move away from emerging market equities in particular at the end of the quarter. US stock markets again reached fresh record highs, but worries mounted over high valuations, with swings in sentiment towards tech stocks in particular. For Q3, the S&P 500 returned 4.5% and the Nasdaq 6.2% (but -0.1% in September).

In the Eurozone, the region's growth accelerated to 2.1% (q/q annualised) in Q2 from Q1's 1.9%, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. CPI at 1.5% in August was also higher than expected, due mainly to rising energy prices, while growth forecasts were revised further upward and the euro appreciated against the US dollar – the currency is 13% stronger against the greenback so far in 2017. Manufacturing PMI data for September in both France and Germany came in at the highest levels in six years. At its September meeting the ECB left interest rates on hold, while paving the way for a tapering of its quantitative easing programme. For the quarter, the Dow Jones Eurostoxx 50 returned 8.5%, while Germany's DAX 30 delivered 7.6% and the French CAC 40 7.8% (all in US$).

Meanwhile, the UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment. The weaker pound over the quarter continued to drive up the cost of imports and inflation: August CPI accelerated to 2.9% y/y, above the 2.8% expected. At its September policy meeting, the Bank of England said its concerns over inflation now outweighed those over Brexit-related risks to the economy, although it left its base interest rate unchanged. The FTSE 100 returned 4.8% (in US$) over the quarter.

In Japan, Q2 GDP growth jumped to 4.0% (q/q annualised), far exceeding the 2.5% expected thanks to strong household consumption and business investment during the quarter. This marked six successive quarters of growth, the longest streak since 2006. However, inflation remained subdued at only 0.9% y/y in August, and excluding energy and food costs was flat. The Nikkei 225 Index returned 2.1% over the quarter (in US$).

In China, Q2 GDP growth surprised to the upside at 6.9% (q/q annualised), unchanged from Q1 and above 2017's official 6.5% growth target, with factory output boosted by improving global trade and higher domestic demand. The upcoming Communist party conference in October meant government and the central bank were focused on maintaining financial market stability, underpinning asset strength for the quarter. The equity market continued its remarkable performance with the MSCI China returning 14.8% in Q3: it has now delivered 43.4% for the year to 30 September.

Other emerging market (EM) assets posted strong returns in Q3 as risk-hungry investors continued to seek out EM equities and bonds, although in September equity demand waned. Overall, the MSCI Emerging Markets Index returned 8.0% in US$ (but -0.4% in September). This compared to 5.0% from the MSCI World Index for developed markets. Among the larger EM equity markets in US$ terms for the quarter, Brazil's Bovespa was the strongest performer with a 23.3% total return, followed by the MSCI Russia (18.1%) and the MSCI China (14.8%). The poorest Q3 returns (in US$) came from the MSCI Turkey (0.4%) and the MSCI India (3.0%). The MSCI South Africa (in US$) produced 4.0%, for a 12.7% return year to date.

In commodities, the price of Brent crude surged some 20.1% during the quarter to around $56.70 per barrel at quarter end, driven by mounting signs that the three-year market oversupply is finally easing on the back of production cuts by OPEC and other producers. Other commodity prices also moved higher in line with accelerating global growth and a weaker dollar towards the end of the period. Gold gained 3.1% largely on the back of North Korean tensions, and palladium rose 11.2%. Platinum, however, lost 1.5% on oversupply concerns. Among industrial metals, the bellwether copper gained 8.5%, zinc was up 16.4%, nickel increased 11.4%, lead rose 9.6% and aluminium was 8.7% higher.

South African equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand.

A major local highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019). The FTSE/JSE All Share Index reached record highs in August before retreating in September, still posting an impressive 8.9% return for the quarter. Gains were led by a 17.7% return from Resources shares on the back of stronger commodity prices, while Industrials produced 7.4% and Financials delivered a 5.1% return. SA listed property returned 5.7%. The rand, meanwhile, weakened fairly sharply in September along with many other emerging market currencies: for the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro.

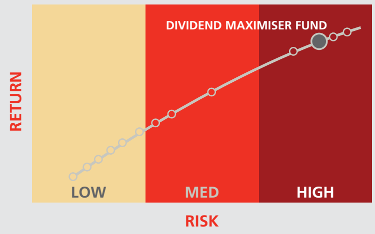
STRATEGY AND POSITIONING

There have been relatively minor changes to the fund's strategy and positioning since Q2. While the fund's holding in Naspers was one of the major contributors to returns (and relative outperformance) during the quarter, its overweight positions in resources groups Anglo American, BHP Billiton, Exxaro and Glencore also added significant value. We continue to believe that these stocks offer more defensive commodity exposure at reasonably compelling valuation multiples, and therefore maintain our overweight exposure.

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	T CLASS	B CLASS
1 year	9.2%	4.2%	9.4%	9.6%
3 years	5.9%	4.2%	n/a	6.4%
5 years	12.2%	9.6%	n/a	12.7%
7 years	12.5%	10.3%	n/a	13.0%
10 years	10.8%	7.8%	n/a	11.2%
Since inception	17.5%	14.2%	4.9%	11.9%

[#] 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 704 083 430

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

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL DIVIDEND MAXIMISER FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

We participated in the listing of local retailer Steinhoff Africa Retail (STAR), which offers attractive - but relatively expensive -exposure to Pep and Ackermans, despite some concerns over governance issues originating from holding company Steinhoff. We remain concerned about the fundamentals, hence an underweight holding in the latter counter. Our interest-sensitive exposure continues to be held via an overweight exposure to SA banks, offset by underweight positions in the general retailers and property sector.

Our offshore industrial exposure is retained through British American Tobacco, Richemont, Bidcorp and Naspers, which make up a high conviction and material proportion of the fund. We highlighted the reasons for these holdings in our previous quarterly report, and continue to believe that these stocks offer better risk-reward payoff profiles than their domestic industrial counterparts. The shift in global consumer behaviour towards digital channels over the past few years is one of the most dynamic and significant trends in many decades, and should not be underestimated. We have, however, recently introduced a somewhat higher risk exposure to enX, an attractively valued small cap industrial stock that offers a reasonable margin of safety to compensate for these risks. We are well aware of a number of small cap failures, particularly in the construction sector, and the stock has underperformed over the short term, but believe that investors will be rewarded over the longer term as earnings from its core industrial distribution and fleet management businesses materialise.

OUTLOOK

As of quarter-end, the market as a whole appears to be trading around fair value, although the current level of earnings looks to be about 20% below trend. We see little scope for a material re-rating in the market, but believe that with the right management intervention, a number of turnaround situations exist, in addition to the previously mentioned opportunities. The road ahead is likely to be bumpy, however. Looking offshore, we still consider some offshore equity markets to be relatively undervalued and attractive, and therefore maintain the fund's offshore exposure.

As has been demonstrated over the past quarter, it is in these uncertain and difficult times that the best opportunities often present themselves. We remain diligent in our search for such opportunities, where the distribution of possible returns and margin of safety justifies a holding in these stocks in a challenging and uncertain environment.

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. ■

Sources: Prudential, Morningstar & Deutsche Securities

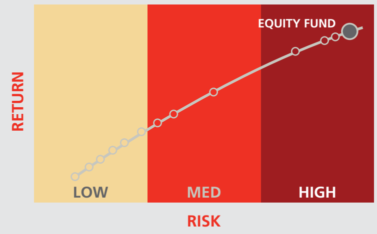
PRUDENTIAL EQUITY FUND
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

RISK/RETURN PROFILE:



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 793 507 585

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

PERFORMANCE

The fund returned 6.9% for the three months ended 30 September 2017, outperforming its benchmark which returned 6.0%. For the past 12 months the fund has outperformed the benchmark by 6.5% with a return of 10.8% versus 4.2%.

The main contributors to returns during the quarter were the fund's overweight positions in Anglo American, BHP Billiton and Exxaro, which returned 42%, 22% and 35% respectively. In prior quarters' commentary we have highlighted our preference for the diversified general miners over single-commodity producers, in particular gold and platinum miners. We remain cautious on the outlook for iron ore prices and expect lower average prices to be realised in 2018. We have, however, maintained our exposure to the above diversified miners because current valuations already discount the lower commodity prices and are offering high double-digit free cash flow yields. We have sought exposure through higher-quality stocks with reasonable margins and strong balance sheets. Ongoing cost initiatives and improved commodity prices have resulted in significant cash flow generation for the miners, with spot commodity prices having been sustained at higher levels than consensus expectations.

We increased exposure to Exxaro in Q1 2017, on the basis of favourable sum-of-the-parts valuation analysis. The sell down of Exxaro's interest in US-listed Tronox has commenced and a new BEE transaction is set to be completed in Q4 2017. We believe that the simplification of Exxaro's structure will lead to a re-rating of the underlying coal business, which has a strong underpin to its future earnings given that Eskom's newly built Medupi will be dependent on coal supplied from Exxaro's Grootegeluk mine.

Whilst the valuation of these three stocks is still compelling on free cash flow yields, the fund has taken some profits and mildly reduced exposure to Anglo American.

Our overweight position in PPC also contributed favourably as the share price rallied nearly 20% during the quarter. Much of this rally followed the announcement of a conditional offer from Fairfax Africa to acquire a R2 billion stake in PPC, on condition PPC accepts a merger with Afrisam. We are not supportive of the offer at current levels as we believe it undervalues PPC, and continue to see significant future value in PPC's African operations in Rwanda, Zimbabwe, Ethiopia and Democratic Republic of Congo. These new production plants have recently been commissioned and are in ramp-up. After two years of falling prices in South Africa, cement prices have started to stabilise, with modest price hikes having been put through in the latest quarter. We believe PPC has the potential to more than double its current earnings over the next three years, and that the offer from Fairfax undervalues these prospects. The proposed merger with Afrisam creates further uncertainty and is likely to have competition remedies imposed, given the dominant market share position of the combined entity.

The Fund has also benefited from being underweight Vodacom, with the share price underperforming over the quarter for a number of stock-specific reasons. Following Vodacom's successful purchase of Vodafone's stake in Kenyan mobile network operator Safaricom, Vodafone was subsequently required to sell just over 5% of its stake in Vodacom in order to restore a 20% free float to comply with the JSE listing rules. The Competition Commission has also launched an investigation into Vodacom's award of a government communications contract worth close to R5 billion over a four-year period.

Among the detractors from the fund's performance included an overweight exposure in Netcare, though in part offset by the underweight exposure to Mediclinic. We are generally neutral the hospital sector. In South Africa the general criteria of medical aid funds for hospital admissions have become more stringent, resulting in a decline in 'paid patient day' traffic for local hospitals. In addition, a soft economic environment and continued regulatory risk remains a significant headwind for the sector.

Our overweight position in the UK property company, Capital and Counties (CapCo) has been adversely affected by both pound weakness and market concerns around the impact of Brexit. CapCo, however, trades at a 25% discount to its NAV, which we believe is a compelling valuation, and we have continued to increase exposure.

Datatec was also a minor detractor over the quarter, despite the company having received an unsolicited bid from US-listed Synnex Corporation for a large portion of its Westcon-Comstar business for approximately US$630 million. Datatec shareholders, including ourselves, have accepted the offer. Following receipt of the proceeds of sale, Datatec intends to distribute US$500m (equivalent to 54% of Datatec's current market cap) of this in the form of share buybacks and special dividends. Although the deal was favourable to Datatec shareholders, we continue to see value in the residual businesses remaining within the Datatec listed entity.

PORTFOLIO CHANGES

The fund has moved to an underweight position in Sasol. Sasol remains heavily dependent on the oil price, which seems currently capped given prevailing supply and demand patterns. Disappointing delays in the Charles Lake ethane cracker project and ongoing costs have postponed potential returns on capital.

The fund has been reducing its exposure to Tiger Brands on concerns the current weak consumer environment and deflationary food prices will negatively impact the company's ability to grow its revenues and meet current 2018 earnings estimates. We view Tiger Brands as being fully valued at the current share price, and offering unattractive prospective returns within the sector. We recognise lower maize prices on the back of a record domestic crop will benefit food producers such as Pioneer and Tiger Brands, however we see the poultry producers, in particular Astral Foods, benefiting more significantly as the primary input cost to production drives a recovery in profit margins.

The fund retains an underweight position within the platinum sector. A potential future theme is the displacement of the internal combustion engine (ICE) with battery-powered electric vehicles (BEVs). Declaring the death of platinum group metals in emissions catalysts is premature, but the case for long-payback capex projects is poor, and premium ratings for long-life assets may be called into question with low cost, well capitalized and cash generative projects being preferred. While the fund currently holds a small position in Impala Platinum, we continue to evaluate this exposure, particularly as the investment case for the platinum sector is heavily dependent on improved PGM prices, which in turn rely on an improvement in the underlying demand for the metals that is potentially threatened by adoption of BEV's.

South African equities became more expensive in Q3, with the FTSE/JSE ALSI 12-month forward P/E rising to 14.6X at quarter-end from around 14X in Q2. However, we remain confident in the portfolio of stocks we have identified, which in aggregate trade at a discount but are projected to deliver similar underlying earnings growth to that of the market.

MARKET OVERVIEW

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	10.8%	4.2%	11.3%
3 years	6.3%	4.2%	6.7%
5 years	12.7%	9.6%	13.2%
7 years	13.2%	10.3%	13.7%
10 years	10.7%	7.8%	11.2%
Since inception	17.5%	14.2%	12.4%

Inception date B Class: 2 January 2007

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

EQUITY

(until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

While growth prospects remained buoyant, data showing higher-than-expected August inflation across the US, UK and Eurozone prompted more hawkish comments from the respective central banks. This, in turn, led investors to expect interest rate tightening earlier than previously anticipated. While this sent developed market equities and currencies higher in September, it sparked sales of US and European bonds, as well as emerging market equities and currencies. In September, South African equities, bonds and the rand all pared their earlier quarterly gains.

Global growth and equity gains continue apace

In the US, Q2 GDP growth was revised significantly upward to 3.0% (q/q annualised) from its previous 2.6% estimate, on the back of higher household spending and business investment. At the same time, September saw: 1) a rise in US August CPI to 1.9% y/y (above expectations and closer to the Federal Reserve Bank's 2.0% target); 2) a clearly more hawkish tone from the Fed; and 3) speculation around the appointment of a more hawkish Fed Chairman to replace Janet Yellen – Kevin Warsh, a former Fed governor. These were among the primary reasons investors moved forward their expectations for the next 25bp interest rate hike to December. With rates anticipated to move higher sooner, US equities and the dollar became more attractive, prompting a move away from emerging market equities in particular at the end of the quarter. US stock markets again reached fresh record highs, but worries mounted over high valuations, with swings in sentiment towards tech stocks in particular. For Q3, the S&P 500 returned 4.5% and the Nasdaq 6.2% (but -0.1% in September).

In the Eurozone, the region's growth accelerated to 2.1% (q/q annualised) in Q2 from Q1's 1.9%, backed by a broad recovery in domestic demand from many euro-area countries, and helped by the European Central Bank (ECB)'s ongoing easy monetary policy. CPI at 1.5% in August was also higher than expected, due mainly to rising energy prices, while growth forecasts were revised further upward and the euro appreciated against the US dollar – the currency is 13% stronger against the greenback so far in 2017. Manufacturing PMI data for September in both France and Germany came in at the highest levels in six years. At its September meeting the ECB left interest rates on hold, while paving the way for a tapering of its quantitative easing programme. For the quarter, the Dow Jones Eurostoxx 50 returned 8.5%, while Germany's DAX 30 delivered 7.6% and the French CAC 40 7.8% (all in US$).

Meanwhile, the UK was growing at roughly half the pace of its EU neighbours, with the slow progress in negotiations over Brexit terms and rising uncertainty hampering investment. The weaker pound over the quarter continued to drive up the cost of imports and inflation: August CPI accelerated to 2.9% y/y, above the 2.8% expected. At its September policy meeting, the Bank of England said its concerns over inflation now outweighed those over Brexit-related risks to the economy, although it left its base interest rate unchanged. The FTSE 100 returned 4.8% (in US$) over the quarter.

In Japan, Q2 GDP growth jumped to 4.0% (q/q annualised), far exceeding the 2.5% expected thanks to strong household consumption and business investment during the quarter. This marked six successive quarters of growth, the longest streak since 2006. However, inflation remained subdued at only 0.9% y/y in August, and excluding energy and food costs was flat. The Nikkei 225 Index returned 2.1% over the quarter (in US$).

In China, Q2 GDP growth surprised to the upside at 6.9% (q/q annualised), unchanged from Q1 and above 2017's official 6.5% growth target, with factory output boosted by improving global trade and higher domestic demand. The upcoming Communist party conference in October meant government and the central bank were focused on maintaining financial market stability, underpinning asset strength for the quarter. The equity market continued its remarkable performance with the MSCI China returning 14.8% in Q3: it has now delivered 43.4% for the year to 30 September.

Other emerging market (EM) assets posted strong returns in Q3 as risk-hungry investors continued to seek out EM equities and bonds, although in September equity demand waned. Overall, the MSCI Emerging Markets Index returned 8.0% in US$ (but -0.4% in September). This compared to 5.0% from the MSCI World Index for developed markets. Among the larger EM equity markets in US$ terms for the quarter, Brazil's Bovespa was the strongest performer with a 23.3% total return, followed by the MSCI Russia (18.1%) and the MSCI China (14.8%). The poorest Q3 returns (in US$) came from the MSCI Turkey (0.4%) and the MSCI India (3.0%). The MSCI South Africa (in US$) produced 4.0%, for a 12.7% return year to date.

In commodities, the price of Brent crude surged some 20.1% during the quarter to around $56.70 per barrel at quarter end, driven by mounting signs that the three-year market oversupply is finally easing on the back of production cuts by OPEC and other producers. Other commodity prices also moved higher in line with accelerating global growth and a weaker dollar towards the end of the period. Gold gained 3.1% largely on the back of North Korean tensions, and palladium rose 11.2%. Platinum, however, lost 1.5% on oversupply concerns. Among industrial metals, the bellwether copper gained 8.5%, zinc was up 16.4%, nickel increased 11.4%, lead rose 9.6% and aluminium was 8.7% higher.

SA returns lifted by bullish global growth sentiment

South African equities notched up their best returns of the year so far in Q3 as the sluggish local economy was offset by strong global demand for emerging market assets, and higher commodity prices buoyed resources shares. Bonds and listed property, meanwhile, were underpinned by an improving interest rate and inflation outlook, as well as keen foreign demand.

A major local highlight for Q3 saw the economy emerge out of recession with Q2 GDP growth of 2.5% (q/q annualised). This was led by a rebound in agricultural production, while manufacturing production and household spending were also higher. However, fixed capital formation was down 2.6% during the quarter, reflecting the ongoing decline in investment this year. Low confidence, slow growth and political uncertainty continue to weigh on businesses despite relatively low capital costs and the positive global environment. In spite of the positive Q2 GDP data, several institutions further lowered their growth forecasts for SA, among them the World Bank (to 0.6% from 1.1% previously for 2017, 1.1% for 2018 and 1.7% for 2019). The FTSE/JSE All Share Index reached record highs in August before retreating in September, still posting an impressive 8.9% return for the quarter. Gains were led by a 17.7% return from Resources shares on the back of stronger commodity prices, while Industrials produced 7.4% and Financials delivered a 5.1% return. SA listed property returned 5.7%. The rand, meanwhile, weakened fairly sharply in September along with many other emerging market currencies: for the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro. ■

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL CAUTIOUS MANAGED FUND OF FUNDS
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL MULTI-ASSET

MARKET OVERVIEW

The global economy continued to grow in the third quarter of the year, as evidenced by data pointing to strong corporate earnings and trade output, supported by a low inflation environment. This was despite markets suffering various geopolitical pressures over the period, as well as central banks hinting at reducing monetary stimulus.

Against this backdrop, global equity markets had another strong quarter in aggregate. Emerging markets generally performed strongly, buoyed additionally by US dollar weakness. Meanwhile, fixed income markets suffered a turbulent quarter, reversing early gains when bond yields rose towards the end of the quarter as central bankers signalled the withdrawal of economic stimulus measures. This environment worked well for the portfolio's positioning in favour of risk assets.

The rand, meanwhile, weakened fairly sharply in September after gains in the previous two months, along with many other emerging market currencies. For the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro. This added to portfolio returns based in rand.

PERFORMANCE

For the quarter ending 30 September 2017, the fund returned 5.6 % (net of fees in rand), outperforming the 4.5% from its benchmark (the average return of the ASISA Global Multi-Asset Low Equity sector). For the 12 months to 30 September 2017, the fund has returned 5.8% p.a., compared to the benchmark's 1.7% p.a.

The main contributors to Q3 2017 performance were exposure to Japan via the M&G Japan Fund and emerging markets exposure via the M&G Global Emerging Markets Fund. Other key equity contributors included the S&P 500 ETF and M&G North American Value Fund holdings.

The portfolio's fixed income holdings also added value, in particular exposure to the M&G European Corporate Bond Fund and to the Eastspring Investments US Investment Grade Bond Fund. ETF exposure to global corporate bonds detracted slightly. The portfolio's small property holding also contributed.

Outperformance in relation to the benchmark was attributable to the portfolio's 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

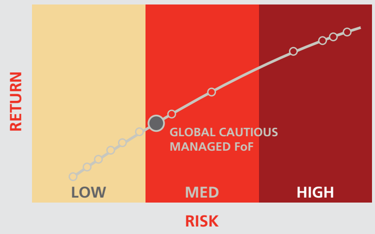
The global macroeconomic picture continues to improve in a reasonably synchronised fashion, with strong economic indicators feeding through to company earnings, in a low-inflation environment. As ever, there is considerable uncertainty in terms of geopolitics, the macroeconomic environment and policy-making, although this is yet to have an impact on asset pricing.

When considering valuations across asset classes in the context of this 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 some emerging market bonds on elevated levels of real yield.

Meanwhile, the improvements in macroeconomic data continue to be reflected in equity markets, which are no longer as cheap as they have been in recent years. This means that we need to be 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. Overall, the large equity risk premium remains the most obvious opportunity on offer today, in our view. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK	B CLASS
1 year	5.8%	1.7%	6.1%
3 years	8.6%	7.8%	8.9%
5 years	12.5%	12.0%	n/a
7 years	11.6%	11.3%	n/a
10 years	6.6%	6.7%	n/a
Since inception	7.9%	7.3%	10.4%

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:

R105 333 557

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL HIGH YIELD BOND FUND OF FUNDS
30 SEPTEMBER 2017

PRUDENTIAL INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL INCOME

PERFORMANCE

For the quarter ending 30 September 2017, the fund returned 4.8% (net of fees, in rand), compared to 4.9% from its benchmark, the Barclays Capital Global Aggregate Bond Index (in rand). For the past 12 months, the fund has returned -1.5% p.a. (net of fees), outperforming its benchmark which returned -3.2%, while over the past five years the fund has returned a net 11.5% p.a., above its benchmark of 10.7%.

The largest contributor to returns for the quarter was the holding in the M&G European Corporate Bond Fund. Positions in the M&G Strategic Corporate Bond Fund, the Eastspring Investments US Investment Grade Bond Fund and ETF exposure to US corporate bonds were the other main contributors to performance. A holding in a Japanese government bond detracted. The portfolio's exposure to global corporate bonds contributed most to the outperformance of the benchmark.

MARKET OVERVIEW

The global economy continued to grow in the third quarter of the year, as evidenced by data pointing to strong corporate earnings and trade output, supported by a low inflation environment. This was despite markets suffering various geopolitical pressures over the period, as well as central banks hinting at reducing monetary stimulus.

Fixed income markets suffered a turbulent quarter, reversing early gains when bond yields rose towards the end of the quarter as central bankers signalled the withdrawal of economic stimulus measures. The Barclays Global Aggregate Bond Index (US$), a mixture of government and corporate bonds, returned 1.8% in the quarter. While US bonds were stronger for much of the period, they erased all of their gains in September. At quarter-end the 10-year UST yield was barely changed at 2.33% from 2.31% at the end of Q2. For US corporate bonds, both investment-grade and high-yield bond spreads narrowed slightly. The portfolio held up well in this environment.

The rand, meanwhile, weakened fairly sharply in September after gains in the previous two months, along with many other emerging market currencies. For the quarter it was down 3.1% against a resurgent US dollar, 6.6% lower versus a rebounding pound sterling, and 6.9% weaker against a resilient euro. This added to portfolio returns based in rand.

POSITIONING

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

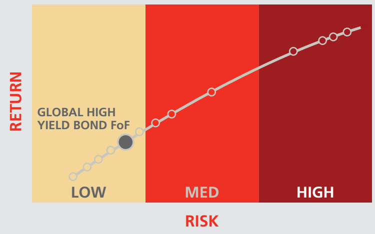
OUTLOOK

The global macroeconomic picture continues to improve in a reasonably synchronised fashion, with strong economic indicators feeding through to company earnings, in a low-inflation environment. As ever, there is considerable uncertainty in terms of geopolitics, the macroeconomic environment and policy-making, although this is yet to have an impact on asset pricing.

When considering valuations across asset classes in the context of this 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 some emerging market bonds on elevated levels of real yield. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	-1.5%	-3.2%
3 years	6.7%	7.5%
5 years	11.5%	10.7%
7 years	12.2%	11.7%
10 years	11.1%	10.5%
Since inception	8.9%	8.9%

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:
R374 283 984

AWARDS:
Raging Bull: 2006, 2008, 2013

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

Sources: Prudential, Morningstar & Deutsche Securities

PRUDENTIAL GLOBAL VALUE FUND OF FUNDS
30 SEPTEMBER 2017

PRUDENTIAL
INVESTMENT MANAGERS

QUARTERLY COMMENTARY

GLOBAL EQUITY

MARKET OVERVIEW

With global growth cementing itself further during the third quarter (Q3) of the year, global equities continued their march higher, putting together the best run in 20 years: six consecutive quarters of gains have been propelled by a combination of accelerating global growth, still-easy monetary policy, subdued inflation and a weaker dollar (until recently). Although emerging market equities lost some steam in September, the MSCI All Country World Index, measuring 46 developed and emerging equity markets, reached record highs.

While growth prospects remained buoyant, data showing higher-than-expected August inflation across the US, UK and Eurozone prompted more hawkish comments from the respective central banks. This, in turn, led investors to expect interest rate tightening earlier than previously anticipated. While this sent developed market equities and currencies higher in September, it sparked sales of US and European bonds, as well as emerging market equities and currencies.

PERFORMANCE

The Fund lagged the benchmark, the MSCI All Countries World Index, by 1.2%, returning +7.3% in Rand over the quarter.

Our underweight to the strong performing EM Asian region detracted from performance as well as our overweight to Turkey. This was in part offset by stock selection gains from our Japan, Pan-European and US fund managers.

STRATEGY AND OUTLOOK

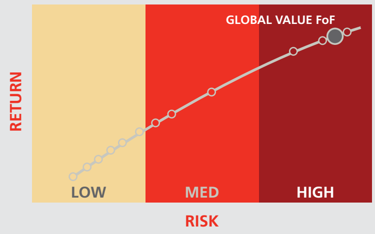
Despite good price gains over the past six quarters and record stock market highs in some countries, the MSCI All Country World Index remains within its "fair value" range with a 12-month forward P/E ratio of 16X at the end of September from 15.8X at the beginning of the quarter – this due to strong corporate earnings growth over the period.

Our current equity positioning reflects a preference for cheaper areas where fundamentals remain encouraging including Europe, Japan, the global financial sector and smaller holdings in selected emerging markets such as Korea, Turkey and Indonesia, compared to global indices and the broad US market. More specifically the top overweight markets comprise South Korea, Germany and Turkey, and top underweights are the US, Canada, Australia and France given their relative high valuations.

In South Korea, for example, after five years of disappointing corporate earnings growth (and downgraded expectations), earnings growth has been surprising to the upside over the past 12 months: while the KOSPI has returned 20.4% in US dollars in the past year, its 12-month forward P/E ratio has fallen from 10.2X to 9.5X to end September thanks to rapid earnings growth. Growth contributors include large tech conglomerates like Samsung which are participating in the global "tech wave" that has sent the US Nasdaq index to record highs. ■

ANNUALISED PERFORMANCE	A CLASS	BENCHMARK
1 year	16.5%	16.3%
3 years	12.5%	14.0%
5 years	20.1%	21.6%
7 years	17.6%	20.0%
10 years	8.5%	11.1%
Since inception	7.1%	8.4%

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:
R262 772 345

Sources: Prudential, Morningstar & Deutsche Securities