UP

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Jewellery will drive the gold price pg 1 | Our manufacturing decline pg 5
Microsoft adapts to a new world pg 8

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01 Jewellery will drive the gold price Jihad Jhaveri

05 Our manufacturing decline Abdul Davids

08 Microsoft adapts to a new world Aslam Dalvi

12 Analysing inflation Justin Floor

15 BC by bike Gavin Wood

17 Performance table

Jewellery will drive the gold price

Jihad Jhaveri - Investment Analyst

"Gold has been mined and treasured for millennia and therefore occupies a unique cultural and psychological position in society. Consequently, an investment in gold is difficult to justify with a rational argument.

Views on gold appear to be sharply polarised. The gold bears regard it as of no use and an asset that yields no cash flow. On the other hand, investors fearful of a future scenario of high inflation and a crumbling world financial system, see gold as the perfect store of value that will withstand any crisis."

Jewellery will drive the gold price

We do not support either of these extreme views. Instead, we carefully analyse likely future supply of gold, above-ground stocks and fundamental demand, which is particularly driven by jewellery demand from the East.

Following a 10-year bull market and a very strong run in the gold price, 2013 has seen a sharp decline in the gold price and a marked increase in price volatility. In this article, we examine the factors contributing to the current volatility in the gold price and give our outlook for the metal price.

Supply of and demand for gold

The estimated composition of above-ground stocks, physical gold that has been mined in the past and is still in use, can be seen in the chart below. A large proportion of this stock is relatively liquid. For example, gold jewellery can be viewed as a quasi-investment with a price elastic[1] recycling market. This means that, at the right price, above-ground stocks can easily meet annual new demand.

As seen in the chart below, 34% of annual supply is currently met by recycling above-ground stocks. The pie charts on the right represent a breakdown of annual supply and demand. Above-ground gold stocks are at least 40 times larger than annual supply and demand (annual flow).

[1] Price elasticity is a measure of the responsiveness of the quantity demanded of a good to a change in its price.

This dynamic makes the gold market unique. Mine supply is not really needed in the medium term. The price of such high existing and liquid inventory levels of gold can therefore decrease far below the average cost of production for a much longer period than with other commodities, where inventory levels are tighter. The durable nature of gold and the fact that it is safely guarded because it is so valuable means that the majority of annual gold production makes its way back to the ever-increasing above-ground stockpile.

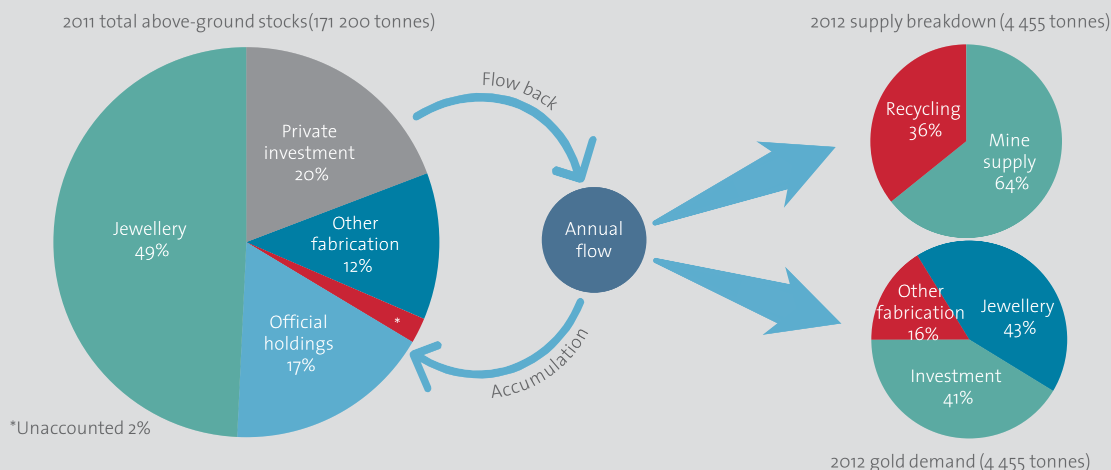
Investment and jewellery demand

Jewellery demand is very price elastic and the 10-year bull market in gold has led to significant demand destruction, with jewellery currently at 43% of total demand - down from a level of over 70% before 2002. High levels of annual investment demand have resulted in high gold prices, which displaced significant amounts of physical jewellery demand.

We have been wary that these high levels of investment demand for gold were not sustainable. Common reasons for investing in gold have been:

- Concerns about ever-increasing levels of monetary stimulus in the developed world causing high inflation in future and the debasement of currencies.

Supply of and demand for gold



Source: Merrill Lynch, GFMS, Thomson Reuters and Kagiso Asset Management research

- Fears around the risk of significant negative financial events. 'Tail risk' events happen without warning and often stem from unexpected sources. However, since the Global Financial Crisis, the 'expected sources' of these tail risks have included concerns about the underlying health of the global banking sector, the sustainability of the Eurozone and high levels of developed world government debt.

We have not believed in the above reasons to invest in gold because:

- There is little evidence that gold is a natural inflation hedge over time and long-term historical analysis is heavily influenced by the starting time point.
- Under a scenario of high inflation, we expect other real asset classes, other commodities and other precious metals (much scarcer than gold) to hold their value in real terms more reliably than gold.

ETF investment demand

Since their formal inception nine years ago, exchange traded funds (ETFs) have been responsible for 23% of new investment demand and 7% of new total demand. The graph below shows the obvious risk to the gold price presented by these high levels of ETF holdings. While they have already grown strongly, for ETF holdings to contribute to annual incremental demand, they have to continue growing. Even a stabilisation of ETF holdings at the relatively high levels of 2012 would mean a complete drop off in an important source of annual demand.

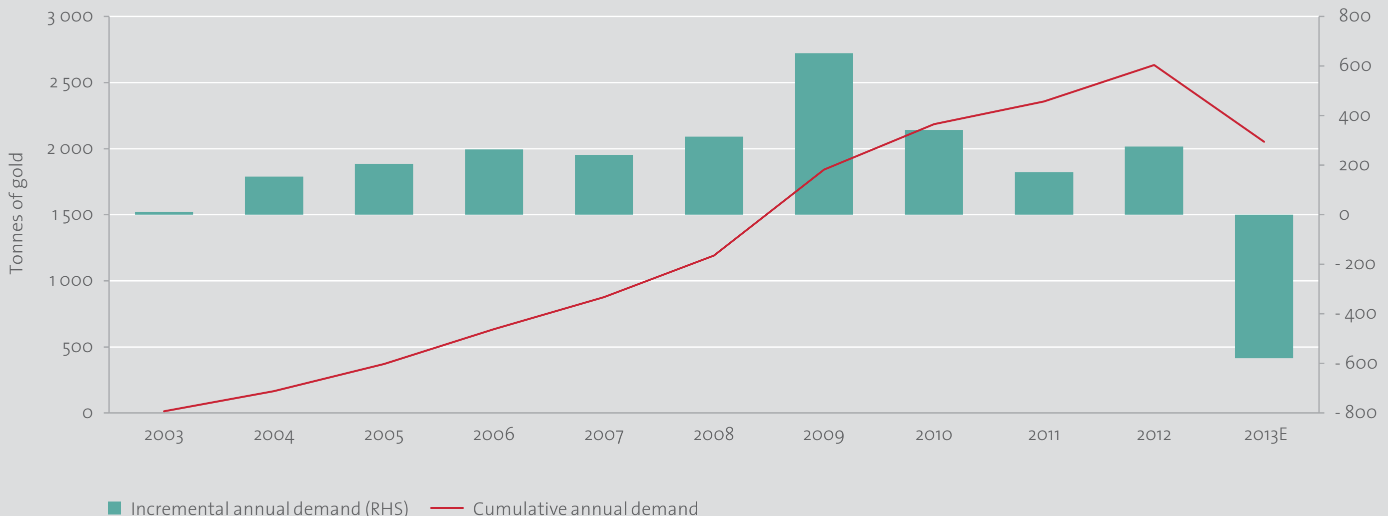
As it turns out, signs of economic stability in developed economies and the prospect of 'tapering' (the inevitable reduction in the US Federal Reserve's quantitative easing programme) seem to have led to a large decrease in ETF holdings in the first half of 2013. This has been the fundamental reason behind the sharp decline in the gold price.

Jewellery is key to the long-term gold price

We believe that the gold market will eventually return to the situation where jewellery will again be the dominant demand source. Due to jewellery's high price elasticity, this will have to be at a gold price significantly lower than that of the recent past. Understanding the jewellery market demand dynamics and the price levels needed to dramatically increase jewellery demand is very difficult to achieve with precision. We therefore prefer to think about a range band for long-term pricing.

Overall, jewellery demand has decreased by 29% over the last 10 years. However, regional statistics show strength in the East,

Global gold ETF demand



Source: Thomson Reuters and GFMS

Jewellery will drive the gold price

with India and China up 20% and 162% respectively over this period. In 2012, India and China comprised 58% of total demand (32% and 26% respectively).

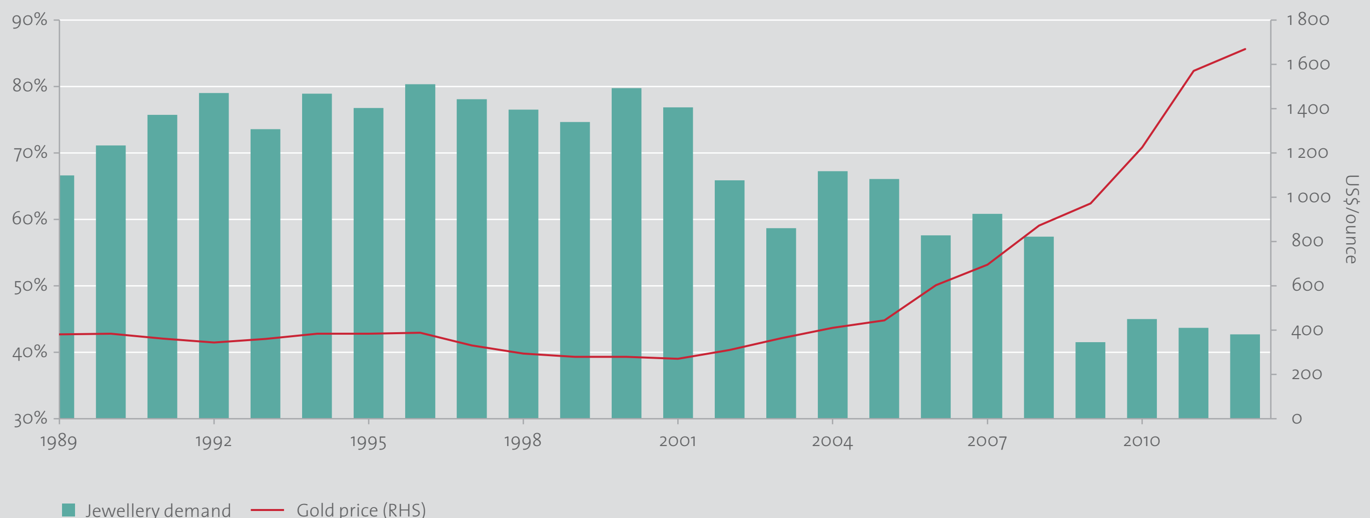
The already healthy levels of Eastern jewellery spend should show steady growth over time in line with increasing incomes. Clearly, the fall in the gold price will lead to more ounces of jewellery demand from the East but the key question is whether jewellery spend (in dollars) will increase sustainably due to the lower gold price. We do not think that this will happen given that many jewellery purchases are made by relatively low income earners who are already spending at their maximum potential. In addition, India is actively trying to control the negative impact of gold imports on its current account. While jewellery price elasticity is not straightforward to reliably model, we believe that jewellery demand will be a powerful force in stabilising the gold supply/demand situation.

India and China

The strong gold investment demand flows during recent years were unsustainable and, consequently, the gold price of the recent past was not a reflection of normalised conditions. We believe that there is a healthy level of Indian and Chinese jewellery demand, which will increase due to a more sustainable (and lower) gold price. This demand will then grow over time.

Uncertainties with estimating the price elasticity of jewellery demand make it difficult to confidently forecast an absolute gold price level. Based on our analysis of the fundamental drivers, our long-term forecast is between US$1 100 and US$1 400 an ounce. However, given the substantial levels of above-ground stocks and the significant sunk capital expenditure in gold mines, and therefore their need to produce all the gold they can if they are merely covering cash costs, we believe that the gold price could overshoot to the downside in the short term. UP

Jewellery demand and the gold price



Source: Thomson Reuters and GFMS

Our manufacturing decline

Abdul Davids - Head of Research

"Over the last decade, South African manufacturers have lost significant market share to China and other Asian low wage cost countries, such as Vietnam, Bangladesh and Thailand. Today, the 'made in China' label is found on most manufactured items as China has entrenched itself as the world's manufacturing hub.

In addition to this competition from the East, South African manufacturers have had to contend with other headwinds that have raised manufacturing costs, thereby eroding the country's global competitiveness."

Our manufacturing decline

The Kagiso PMI

The Kagiso Group sponsors the Purchasing Managers' Index (PMI), a monthly survey of purchasing managers at the country's leading manufacturing businesses. An index reading above 50 indicates that the local manufacturing sector is expanding, while a reading below 50 points to a contraction. This survey is a key measure of conditions in the manufacturing sector and is useful because it is published immediately after the relevant month end.

Since 2009 (when manufacturing output rebounded following the Global Financial Crisis) manufacturing activity has trended lower and has been volatile amid very weak global economic conditions and weak demand for locally manufactured goods.

Listed manufacturers

The country's listed manufacturers operate in a range of sectors, including oil and gas, chemicals, metal beneficiation, automobiles and food and include listed companies like Sasol, Tiger Brands and ArcelorMittal South Africa.

In our portfolios, we have holdings in Sasol, AECI (chemicals and explosives) and Metair (automobile components and batteries).

Why manufacturing is under pressure

The key reasons for the decline in the local manufacturing sector are:

- an uncompetitive labour force;
- high and rising administered prices; and
- globally uncompetitive logistics costs.

Uncompetitive labour

An increase in labour costs without an accompanying rise in labour productivity is the main cause of the manufacturing sector's deteriorating global competitiveness. Labour costs typically account for more than 50% of manufacturers' costs. South Africa has in the past had far higher unit labour cost growth relative to emerging market peer group countries. Much of the blame for this lies with South Africa's very inflexible labour regulations and the power of trade unions.

This is further compounded by South Africa's significant lack of economies of scale, given the size of the country's manufacturing base and labour force, resulting in an ever-increasing labour bill being spread over a small and declining base of produced units. This gives rise to steep inflation in unit labour costs.

Prior to the rand weakening over the last year or so, South Africa was uncompetitive on labour costs and worsening relative to competing countries (for our domestic market via imports and for the global market via our manufactured exports). With the recent significant rand weakness, the country's labour competitiveness has improved and the manufacturing sector should already be feeling less import competition and more competitive export pricing.

Despite widespread unemployment, South Africa has a poor and declining skills base, partly due to the historic imbalances in education spending. There is an urgent need for better education and training at all levels, from primary school to technical colleges and on-the-job apprenticeships to redress the imbalances in the labour market.

Administered prices

In addition to escalating labour costs, local manufacturers face significant increases in administered prices such as electricity and fuel. Successive electricity price hikes over the last few years have transformed South Africa from being one of the cheapest electricity countries to one of the more expensive. These price increases have battered manufacturers' profitability and have resulted in electricity becoming a substantial component of their total cost base.

The graph (left) on the next page highlights the growth in electricity prices relative to consumer price inflation. After below-inflation price increases for the 17 years up to 2007, prices have escalated to record levels in the last five years. Manufacturers that previously relied on 'cheap' electricity no longer have this competitive advantage and both local and export markets are increasingly being supplied by lower-cost producers in the East.

An extreme example of this is the local ferrochrome smelting industry, which has declined significantly in response to the higher electricity costs. It has of late been more profitable for manufacturers operating in this sector to have Eskom pay them for not using their electricity quota than for them to operate at full capacity.

Steep increases in the local price of diesel, due to high global oil prices and the weak rand, have caused further cost pressure for those manufacturers that consume the fuel.

Logistics costs

South Africa's vast landscape means that manufacturers are often located far away from shops where their customers need their goods, both locally and abroad. This makes logistics costs and efficiencies a key consideration. State-owned entities such as Sanral and Transnet have historically underinvested in road, port and rail infrastructure. This underinvestment results in less efficient logistics services, longer turnaround times and the need for more costly alternatives to be used. Airports Company of South Africa has arguably overinvested in airport infrastructure recently and has therefore raised the costs of airport usage to unnecessarily high levels to recoup the cost of this investment. These costs need to be absorbed by manufacturers, adding to their already substantial cost burden.

Financial impact

The graph on the right shows how manufacturers' profitability has been hurt by a decline in gross profit margin, as direct input costs have risen. However, more important is the decline in operating profit margin, which has been negatively impacted by rising labour, energy and logistics costs. The grey shaded area represents the escalating operational costs for manufacturers (such as wages and electricity costs). Operating profit margins are currently at their lowest levels in 42 years.

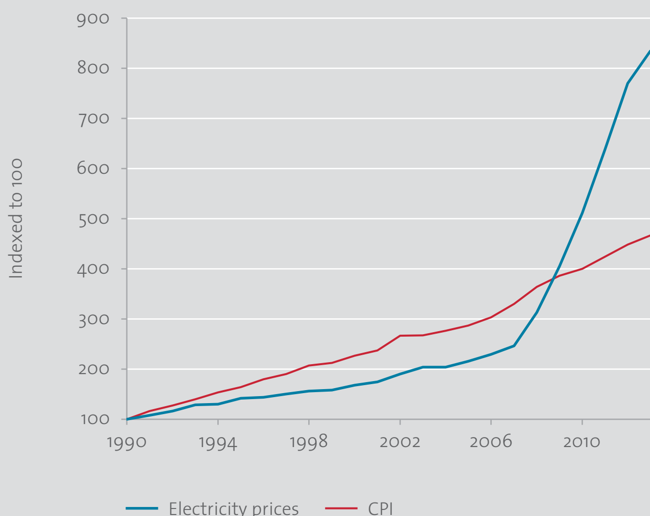
The way forward

South Africa has a world class tertiary sector (including financial services, retail and telecommunication) and a world class primary sector (mining and agriculture) but a very thin and uncompetitive secondary sector (manufacturing and beneficiation). This was not always the case and there is no natural reason for our manufacturing sector to be uncompetitive now.

Faced with this decline in South African manufacturing, our government's response seems to be more intervention, via industrial policy, rather than less. We strongly believe that a government, regardless of how well intentioned, is not in a position to determine where we will be competitive in the world in the long term. It should rather be left to market forces to allocate resources.

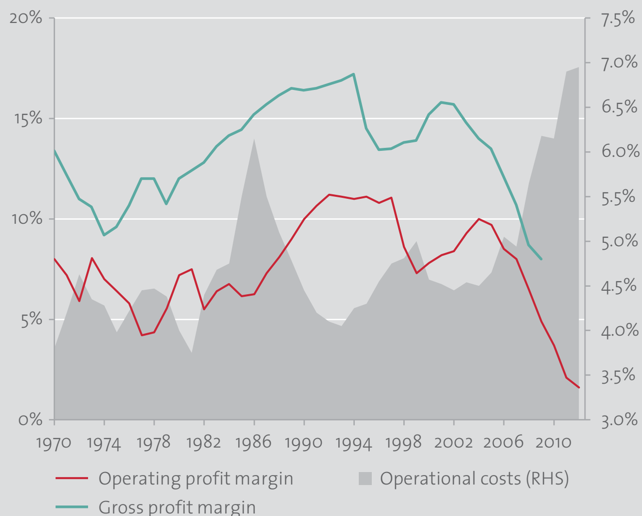
Instead, our government needs to create an enabling environment for the manufacturing sector through a better education system and better skills development programmes to train the country's unskilled workers and through supporting a more flexible labour market that could absorb surplus labour. It could also focus on more effective infrastructure delivery such as roads, electricity, rail and ports, all of which would benefit our manufacturers and help to make them more globally competitive. UP

Electricity prices and the CPI



Source: I-Net and Kagiso Asset Management research

Manufacturers' profit margins



Source: Quantec and Macquarie Research

Microsoft adapts to a new world

Aslam Dalvi - Investment Analyst

"Microsoft is the world's largest software company, best known for its Windows operating system. The company was established in 1975 as a partnership between Bill Gates and Paul Allen.

In 1980, Microsoft distributed its first command-driven operating system, MS-DOS and, in 1985, it shipped the first version of Windows. This marked the start of a very successful growth phase as Windows was universally adopted as the preferred operating system."

The company today has a market share of about 92% of the personal computer (PC) operating system market and a 95% share of the business productivity market - making it a powerhouse in the software industry. In addition, Microsoft has successfully expanded and is now a leading software provider in cloud services, database management and PC development software.

Despite its focus on software, changes in the hardware industry are very important for Microsoft. Given the lack of success their mobile strategy has had to date, the recent shift away from traditional PCs to mobile devices has negatively affected the business and remains a concern. Despite short-term headwinds from an evolving PC industry, the medium-term fundamentals for the business remain attractive.

Microsoft has dominant market shares in key business units, which provide the company with substantial economies of scale. It has limited competition in its traditional markets and there is still low PC penetration in emerging markets, which provides scope for further growth. The company has strong underlying cash flow generation and is available to investors at a bargain price. After careful analysis, we believe Microsoft is a very attractive investment.

More than just Windows

Microsoft has five divisions. The Business division, which accounts for roughly half of the group's profits, is the largest. This division's profits are largely generated from the sale of Microsoft Office and Microsoft Exchange to corporates.

The Windows division, which generates income from the sale of the well-known Windows operating system, is the second largest division and accounts for around 30% of profits.

The Server and Tools (S&T) division sells business-critical software such as SQL server and Visual Studio. This division now accounts for around 25% of profits, having grown rapidly over the last few years. Strong growth in the server and cloud market should result in this division overtaking the Windows division as the second largest in terms of revenue over the next two years.

The fourth division, Entertainment, houses the company's Xbox hardware and related services offering and currently accounts for around 3% of profits. The fifth division, Online Services, is currently loss-making, reflecting the company's efforts to challenge the more established search providers such as Google and Yahoo through its Bing portal and MSN service offerings.

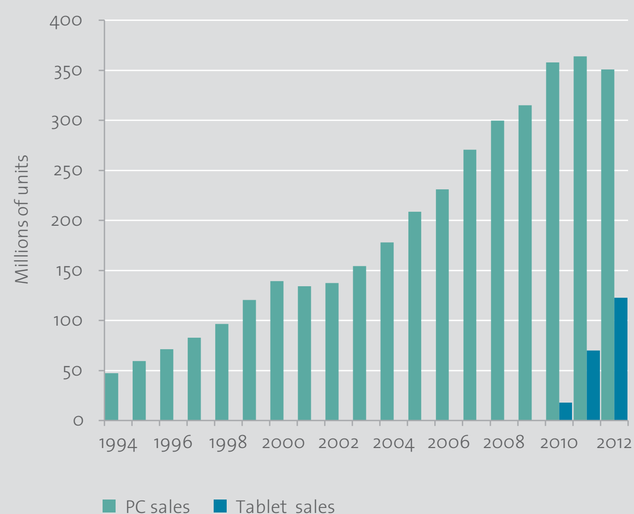
Pressure on Windows

Windows is the dominant desktop and notebook operating system with an estimated market share of around 92%. Operating system development is complex and resource intensive and, as a result, there are few competitors globally. Low competition, combined with a dominant share, provides Microsoft with significant scale benefits. This is reflected in its high operating margin of around 63%.

Despite these fundamental strengths, the Windows division has been under pressure over the last two years as technology usage shifts away from computers to mobile devices such as tablets and smartphones. While Microsoft is dominant in the PC market, the mobile market is led by Google with its Android operating system, which we estimate has a 80% share of the market. The shift away from PCs is clearly visible when looking at industry sales in the chart below.

Data from Gartner shows that PC sales declined by around 4% in 2012 and estimates are for sales to decline by another 11% this year. It appears that the pressure is most acute in the

Annual worldwide PC and Tablet sales



Source: IDC, Gartner and Barclays Research

Microsoft adapts to a new world

consumer or retail market, while the corporate PC market remains relatively resilient.

Tablets are arguably more convenient for simpler tasks such as social media activity, browsing and email, whereas the more demanding needs of a corporate environment (such as higher storage and higher speeds) are best served by a traditional PC. We estimate that around 65% of Windows sales are to the Original Equipment Manufacturer channel, with a large portion of these sales going into the consumer market. Therefore, despite good demand from corporate customers, the Windows division will likely face continued sales pressure over the coming years.

Despite these pressures, the longer-term outlook for PC demand is less negative. Data from the International Telecommunication Union highlights that there is significant room for growth in PC demand from emerging markets, where the number of households with computers is around 24% compared with 65% for the developed world.

Core of the business remains attractive

While prospects for the Windows division are concerning, the outlook for the Business and S&T divisions remains very attractive.

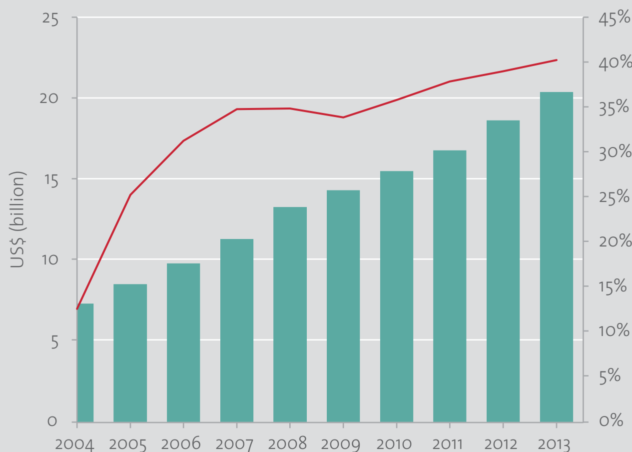
We estimate that around 90% of profits in the Business division are derived from corporate customers, where demand is expected to remain strong. While competition has increased from companies such as Google, competitors have made little progress in the corporate market, given the 'stickiness' of demand, as corporate customers are already heavily reliant on the Microsoft productivity eco system.

Growth for the S&T and Business divisions has been strong, with profits rising by a compound annual rate of 18% and 7% respectively since 2006 (see charts below). Medium-term growth for these divisions will be supported by strong growth in the data and cloud services market.

In addition, we believe that large corporates have significantly underinvested in capital replacement over the last decade, despite their excellent financial health (see charts on the next page). IT firms such as Microsoft are well positioned to benefit as corporates start to replace their ageing IT infrastructure.

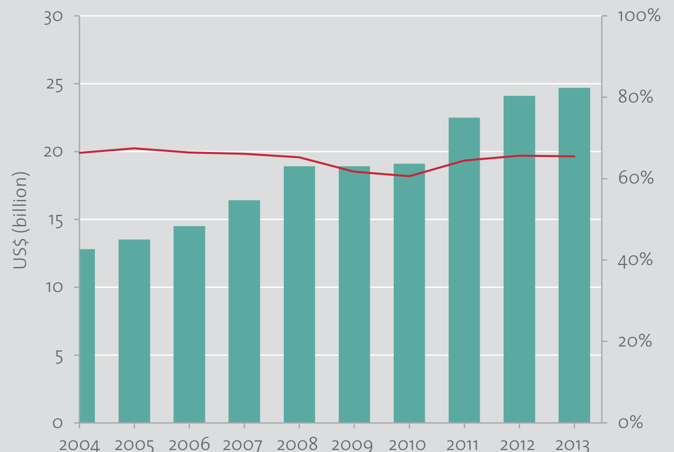
While the proliferation of mobile devices is a direct threat to Microsoft Windows, these new devices present a good opportunity for Microsoft's fast growing cloud services such as Office 365 and Windows Azure.

Server and Tools division



Server and Tools revenue — Server and Tools operating margin (RHS)

Business division



Business division revenue — Business division operating margin (RHS)

Source: Kagiso Asset Management research and Citigroup

Microsoft currently commands a relatively small share (3.3%) of the direct mobile market. The recent acquisition of Nokia presents a unique opportunity for the company to accelerate its mobile share and build on its current position. Given that an estimated 2.3 billion smart devices will be sold in 2014, this opportunity could potentially be material for Microsoft if it is able to win market share from the current market leaders.

Entertainment division

Revenue in the Entertainment division comes from sales of Microsoft's Xbox gaming console and related services such as Xbox Live. Microsoft is the second largest global player, with an estimated 47% market share of the current generation console market.

In November 2013, Microsoft will launch its new console, the Xbox One. This includes functionality such as an integrated movement sensor to control television sets with gestures and voice commands, customisable live sports screens and seamless integration of televisions with other Windows 8 devices.

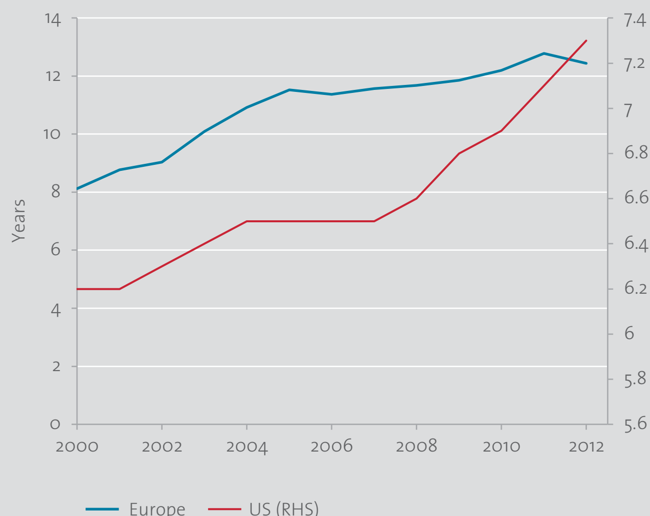
Microsoft is in a strong position with an already established Xbox Live subscriber base of around 46 million users. Current profits are relatively small, but there is potential for good growth as Microsoft focuses on its strategy to 'own the living room' and become the media device of choice for delivering multimedia content to viewers.

What are we paying for?

Despite concerns around declining PC sales and mobile strategy execution, Microsoft represents an attractive investment opportunity. The Business and S&T divisions have solid fundamentals with an attractive outlook and there is potential upside (optionality) if the company successfully carries out its mobile and entertainment strategy.

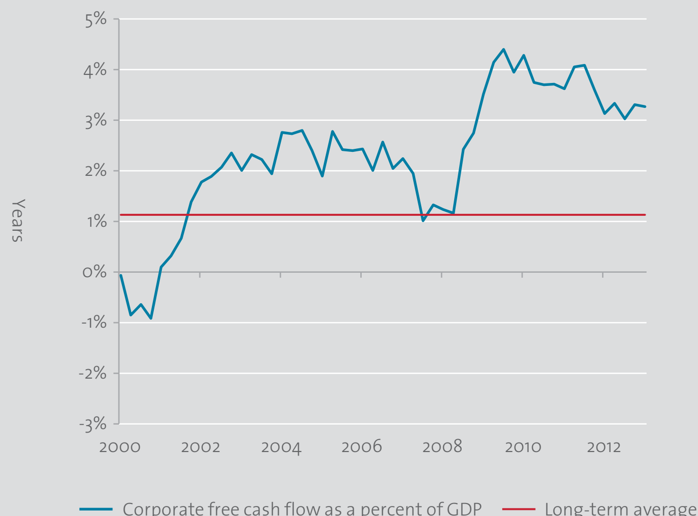
Microsoft has a strong balance sheet with an estimated US$80 billion cash balance. This is around one third of its market capitalisation. Adjusted for this cash and related tax, the company is trading on a single digit price earnings multiple. At current prices, investors are only paying for the Business division, the S&T division and the cash while getting the Windows division and the mobile and entertainment optionality for nothing. UP

Average age of corporate stock: US and Europe



Source: US Bureau of Economic Analysis and Credit Suisse

Free cash flow as a percent of GDP



Source: Bloomberg and Credit Suisse

Analysing inflation

Justin Floor - Investment Analyst

"Inflation is the continuous, general increase in the prices of goods and services in an economy. Inflation has an important effect on asset prices and therefore significant changes to inflation expectations can have a material impact on markets. It is a fundamental feature of any global and domestic macroeconomic analysis.

Inflation has the potential to profoundly affect individual consumers through the gradual erosion of purchasing power over time if income growth is lower than inflation."

Consumer inflation is generally the most commonly understood form of inflation and relates to those prices directly affecting consumers. Other perspectives of price increases also exist, such as wage inflation, which measures the increasing level of wages. The GDP deflator is yet another form and measures the difference in real and nominal production across the entire economy, taking into account price increases for all sectors of the economy, including the consumer sector.

Measuring inflation

The most commonly used metric to measure consumer inflation is the Consumer Price Index (CPI), calculated by Stats SA. CPI measures the change in the price level of a pre-determined basket of consumer goods and services on a monthly basis. This basket (see current weights in the chart below) attempts to represent an average consumer.

However, due to the fact that the basket is formed by averaging across a spectrum of consumers with different income levels, this 'average consumer' does not in fact exist. For example, a low-income consumer's basket would have a much greater weighting for food and public transport than the average, while a higher-income basket would have a greater weighting in services and recreation.

Causes of inflation

The causes of inflation are complex, multidimensional and difficult to forecast over the short term.

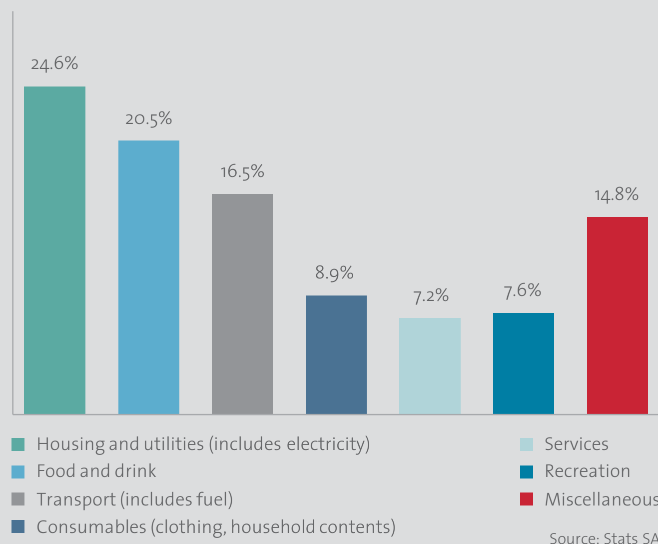
Keynesian explanations for inflation may work through supply shocks, whereby prices are 'pushed' upwards through higher costs. Alternatively, increased levels of demand in an economy can act to 'pull' prices upwards. Second-order expectations of future inflation can also be inflationary. For example, wage negotiations (which eventually feed through to some prices) often depend on expectations of future inflation.

Monetarist explanations for inflation are linked to the growth in the supply of money and the pace of economic activity. Central banks influence money supply (and thereby inflation) through several policy tools. These include setting the repo rate and banking sector reserve requirements, which influence credit extension through changing the cost of borrowing. Direct money market interventions, such as the buying and selling of treasury bills, can be used as a further tool to create and absorb money supply directly.

Currency impact

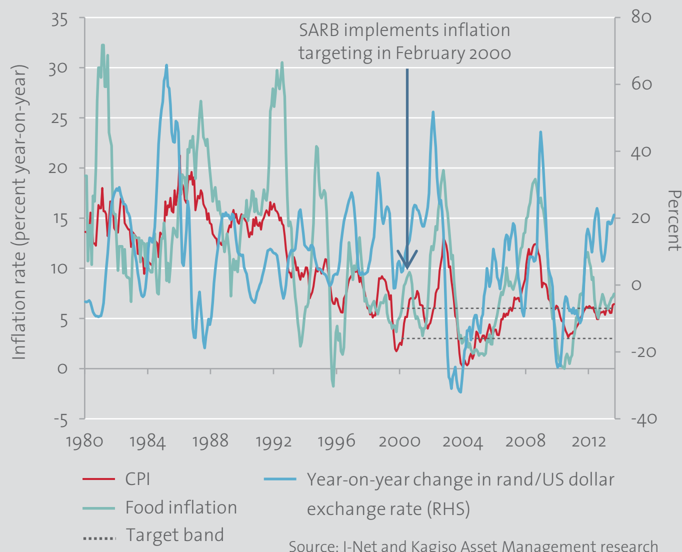
In a small and open economy like South Africa's, inflation's destiny is inextricably linked to changes in the level of the exchange rate. A depreciating currency eventually leads to

Current CPI basket weights



Source: Stats SA

A history of consumer inflation in South Africa



Source: I-Net and Kagiso Asset Management research

inflation as higher costs of imported goods and services are reflected in consumer prices. For example, higher fuel prices and more expensive vehicle prices are soon felt after a period of currency depreciation.

The South African Reserve Bank (SARB) estimates that for every 10% depreciation in the currency, the 'pass-through' to CPI inflation should be around 2%, albeit with a time lag of around nine to 10 months.

Inflation targeting

Generally accepted economic theory holds that inflation is dangerous at the extremes and best results are obtained in moderation and with stability.

If inflation is too high, it can lead to undesirable outcomes in an economy, such as losses in real terms to savers and those with fixed incomes, increased price speculation crowding out production, wastage of resources on implementing price changes (eg menus at restaurants) and heightened socio-economic tension and disruption. In very rare cases hyperinflation, as witnessed in post-war Germany (1921 to 1924) and recently in Zimbabwe (2008 to 2009), can severely damage an economy.

The opposite extreme, highlighted by the Japanese example, is where deflation - continuously falling prices - leads to stagnant economic activity. This can be attributed to a high incentive to save outweighing the incentive to invest in economic production and to spend generally.

Interestingly, this implies that some inflation is in fact desirable and moderate inflation is a requirement for sustainable economic growth.

For these reasons, the SARB was given an inflation targeting mandate in February 2000 to aim for headline CPI inflation between 3% and 6% . The relatively wide band provides policy flexibility appropriate for a developing economy, and the reasonably high level of the band reflects the structurally higher level of inflation common to emerging economies.

Implications

As can be seen in the graph on the right (previous page), consumer inflation was at very elevated levels, averaging somewhere near 15%, until the implementation of inflation targeting. Since then, the SARB has done an admirable job in taming inflation, in spite of challenges presented by key inflation drivers such as the currency and food inflation, which have shown significant volatility over the last 13 years.

More recently, local inflation has been increasing, with the headline CPI rate rising to 6.4% in August, above the 6% upper threshold of the target band. Risks for sustained high inflation are present as a weakening currency, above-inflation wage settlements and higher administered prices continue to feed through to consumer prices.

Globally, consumer inflation is remarkably absent from the system in spite of an exponential growth in money supply as a result of global monetary stimulus. We would argue that this is due to lacklustre levels of global economic activity. It seems that the excess liquidity in the world has instead contributed to another type of price increase - asset price inflation.

Managing the inflation threat

As investment managers, we need to be vigilant of the threat of inflation. Clients invested in our multi-asset class funds benefit from our team's best investment ideas across local and international equities, property, inflation-linked bonds and commodities. These asset classes are relatively protected against inflation - either because their intrinsic cash-flows adjust to inflation over time, or because the tangible nature of the asset is expected to retain its value in real terms.

Ultimately, however, we believe that the best defence against inflation is to avoid the permanent capital loss that arises from overpaying for investments that have been unduly subjected to the unnatural forces of asset price inflation present in the world today.

Our philosophy of carefully assessing the valuations of investments based on cash flow generation potential is leading us to avoid those segments of the market which have become most overpriced. This gives the portfolios further protection against inflation's eroding effect over time. UP

BC by bike

Gavin Wood - Chief Investment Officer

"If you were to take a globe map of the earth and try to find the furthest holiday destination from Cape Town, you would end up with Vancouver (or maybe Hawaii).

We chose Vancouver in beautiful British Columbia (BC), Canada's westernmost province, because it is the starting point for one of the world's most scenic and technical mountain bike stage races."

BC by bike

Canada

Canada is the second largest country in the world, with a total area some eight times the size of South Africa. The maple leaf country is a constitutional monarchy, with Queen Elizabeth II as head of state, and has two official languages stemming from its 16th century colonisers, England and France. The country's name originates from the St. Lawrence Iroquoian word 'kanata', which means village or settlement.

Canada is a member of the G8 and has the ninth highest global per capita income, with a relatively low level of income disparity. Its service industry employs about 75% of its workforce, but it has an unusually large primary sector for a developed country. Petroleum (it has 13% of the world's oil reserves) and logging are the largest components, but it also produces zinc, uranium, gold and other mined minerals. Its manufacturing sector is mostly in Ontario and Quebec, with automobiles and aeronautics as key products.

Canada's population of approximately 35 million is ethnically diverse and distinctly multicultural, a result of significant (and currently rapid) immigration from many countries. The US, with which Canada shares the world's longest common border, has also had a significant influence on Canada, with about 80% of Canadians living within 150 kilometres of the US border. We found Canadians to be extremely friendly and helpful - so much so that it was impossible to walk down the streets holding a map out without being stopped many times over with earnest offers of assistance.

British Columbia

BC is a beautiful land of endless mountains, trees, water and islands - 75% of the province is mountainous (mostly the Rocky Mountains) and 60% is forested. It is no wonder it is a large recipient of tourists and immigrants, especially more recently from Asia. Property is consequently expensive, with some even calling a housing bubble. We encountered an interesting contradiction between 'wealthy', older landowners living frugally as they do not have much income, and younger people, who earn higher incomes, being unable to afford houses at all.

The largest city in BC is Vancouver, which has consistently been voted one of the world's best cities in which to live. It hosts the headquarters of many large natural resource companies and has a film industry, known as Hollywood North, which is the third-largest feature film production location in North America. It is a city surrounded by tall mountains that are snow-capped even in mid-summer. Large bridges, massive ferries and seaplanes help the populace traverse its vast waters.

The BC Bike Race

This race attracts some 540 riders from all over the world, including this year: (only) 120 Canadians, over 100 Mexicans and 18 South Africans. We lined up with rented long-travel trail bikes, with fat tyres and dropper seatposts, ready for the famed singletrack. We were not disappointed and were, in fact, challenged to our limits by amazing forest trails. We confronted endless tree roots that broke our rhythm and tired us out, death-defying steep descents on which it was impossible to stop, long and steep switchback climbs and narrow log bridges across deep drops.

Given that we were riding in the wilderness, the organisers warned us what to do if confronted by a black bear (back away slowly without making eye contact and drop into a submissive foetal position if charged) and that there was not much one could do if confronted by a grizzly bear. We needed to pack safety whistles and waterproof matches in case we lost the track.

Only twice did we ride from the same place where we finished the day before, with most of the days including a bus trip and sometimes also a ferry ride. This meant that we were always riding on pristine, testing mountain biking trails, with no dull transition riding. The riding highlights were possibly the seemingly never-ending downhill trails in Squamish and the final day in the Whistler bike park, with its 'big air' jumps and large berms.

Coming back home to Cape Town from abroad is not usually as difficult as it was this time returning from beautiful BC. Our local trails also no longer seem so technical nor steep. UP

Kagiso Asset Management Funds

Performance to 30 September 2013	1 year	3 years[1]	5 years[1]	Since launch[1]	Launch	TER[2]
Unit trust funds[3]						
Equity Alpha Fund	27.8%	15.9%	17.0%	22.5%	26-Apr-04	1.50%
South African Equity General funds mean	22.7%	15.3%	14.0%	17.3%		
Outperformance	5.1%	0.6%	3.0%	5.2%		
Balanced Fund	19.8%	-	-	13.7%	3-May-11	1.63%
South African Multi Asset High Equity funds mean	18.7%			13.4%		
Outperformance	1.1%			0.3%		
Protector Fund	11.2%	6.8%	7.7%	11.2%	11-Dec-02	2.17%
CPI + 5%[4]	10.4%	10.5%	10.1%	10.7%		
Outperformance	0.8%	-3.7%	-2.4%	0.5%		
Stable Fund	11.8%	-	-	9.6%	3-May-11	1.64%
Return on large deposits*	5.0%			5.3%		
Outperformance	6.8%			4.3%		
Institutional funds[5]						
Managed Equity Fund	28.1%	17.6%	17.9%	15.9%	1-Sep-06	
FTSE/JSE SWIX All Share Index	25.3%	18.3%	17.1%	14.6%		
Outperformance	2.8%	-0.7%	0.8%	1.3%		
Core Equity Fund	29.1%	18.9%	17.9	20.6%	1-Nov-04	
FTSE/JSE SWIX All Share Index	25.3%	18.3%	17.1	19.6%		
Outperformance	3.8%	0.6%	0.8	1.0%		
Domestic Balanced Fund[6]	15.0%	13.1%	12.2%	9.9%	1-May-07	
Peer Median[7]	16.7%	16.0%	13.2%	10.5%		
Outperformance	-1.7%	-2.9%	-1.0%	-0.6%		
Global Balanced Fund[8]	-	-	-	-	1-Jul-13	
Peer Median[9]						
Outperformance						
Sharia unit trust funds[3]						
Islamic Equity Fund	22.4%	13.6%	-	17.1%	13-Jul-09	1.30 %
South African Equity General funds mean	22.7%	15.3%		18.2%		
Outperformance	-0.3%	-1.7%		-1.1%		
Islamic Balanced Fund	17.0%	-	-	8.8%	3-May-11	1.63%
South African Multi Asset High Equity funds mean	18.8%			13.3%		
Outperformance	-1.8%			-4.5%		

1 Annualised; 2 TER (total expense ratio) = % of average NAV of portfolio incurred as charges, levies and fees in the management of the portfolio for the rolling 12-month period to 30 September 2013; 3 Source: Morningstar; net of all costs incurred within the fund; 4 CPI for September 2013 is an estimate; 5 Source: Kagiso Asset Management; gross of management fees; 6 Domestic Balanced Fund and benchmark returns to 31 August 2013; 7 Median return of Alexander Forbes SA Manager Watch: BIV Survey; 8 Performance will be published after 6 months from inception (launched 1 July 2013); 9 Median return of Alexander Forbes Global Large Manager Watch. * Return on deposits of R5 million plus 2% (on an after-tax basis at an assumed 25% tax rate).

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