Skyblue Fund Feedback

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Dissecting November 2019

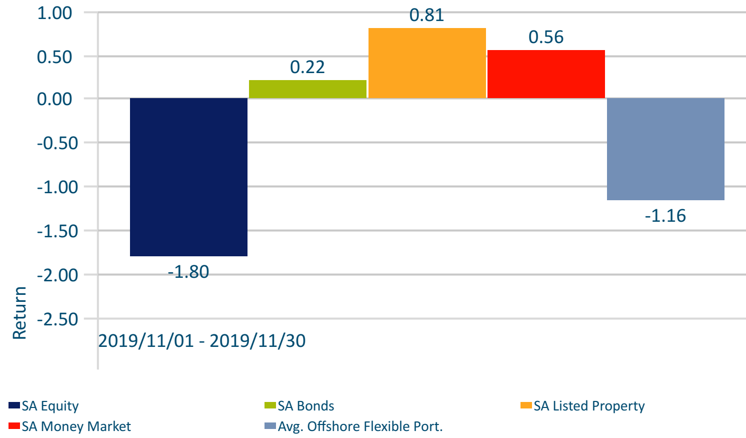
November was a positive month for most global markets, as indices across US, Europe, and UK posted strong gains. Losers included China and South Africa, with China experiencing an unexpected drop in exports over the month, reflecting the strain of ongoing tariffs in an already weak global demand environment. The Chinese manufacturing sector however posted upbeat data. Prospects for a positive outcome in trade negotiations resurfaced on comments emanating from both parties, but became uncertain again towards month-end when US President Trump signed legislation backing Hong Kong protesters. The 15 December deadline for additional tariffs will be a critical indication of progress.

Despite various disappointing and concerning news reports, both globally and locally, the Rand has been trading in a relatively narrow band, and showed a strengthening trend throughout the month to end at R14.67, down from just over R15 to the US Dollar the previous month. Clearly, there has been some pent up margin in the currency, and investors are potentially looking past the "headlines" for now, given the forgiving global environment present in November. However, clear risks remain for the currency, albeit relatively short term. If the February budget shows further fiscal deterioration without a "to the point" plan of action, resulting in a downgrade by Moody's to junk, the Rand may well join the parachute regiment!

With the above in mind, despite positive returns in US Dollars, offshore returns priced back to Rands were negative for the month, with the average offshore flexible portfolio losing 1.16%. SA Equity was an even bigger detractor however, as market heavyweights Richemont, AB InBev, Naspers, and Prosus all lost significant ground, pulling the index down. The other asset class returns were relatively muted, with SA Listed Property being the best performer, delivering 0.81%, followed by SA Cash (0.56%), and SA Bonds (0.22%).

Asset Class Returns - November

Currency: South African Rand



Calendar Year Returns - Annualised (%)

	1 Year	3 Year	5 Year	10 year
SA Equity	13.08	6.61	5.26	10.74
SA Bonds	9.00	9.30	7.03	8.78
SA Property	2.98	-1.70	1.86	11.24
STeFI Composite ZAR	7.31	7.38	7.18	6.52
(ASISA) Global MA Flexible	16.47	8.36	9.14	11.48

*Annualised return is the weighted average compound growth rate over the period measured.

A few highlights from local economic data for the month included inflation dropping to the lowest level since 2011, coming in at 3.7% year-on year. In the last MPC meeting for the year, the SARB decided to leave the repo rate unchanged at 6.5%, although the pressure to cut is growing in the low growth low inflation environment.

Some Food for Thought

For this month's food for thought we decided to shed some light on a hot topic in the investment arena, active vs passive investments. Globally the trend has lately been in favour of passive/index tracking funds, with almost half of the US equity market now comprising index funds. As we know, this market is much bigger, and believed to be more efficient, than our local market - so one has to ask the question whether our local active managers can exploit the perceived inefficiencies that make for the active investment case, and produce alpha over time (which the US public seem to be doubting of their active managers).

We decided to focus on the four major asset classes SA Equity (ASISA SA Equity General), SA Bonds (ASISA SA IB Variable term), SA Property (ASISA SA RE General) and SA Cash (ASISA SA IB Short Term) from 2004 to 2019. To measure the relative performance of active managers we looked at the following areas of potential value add: 1) Do Active managers outperform Passive Investment over time? 2) Can the case be made for Active managers in different market conditions?

In order to measure the number of times that active managers have generated positive alpha, each active manager's performance was measured relative to the respective index over the 15 year measurement period. The average outperformance for each active manager was then calculated over the measurement period and tallied along with the other active managers to arrive at the overall probability of outperforming the index over a 1 year and 3 year period. The chart breaks the % of times the active managers were able to outperform the passive investment into ranges on the x-axis, with the y-axis indicating the % of active managers falling within each range.

Skyblue Fund Managers (Pty) Ltd.
7th Floor, Letterstedt House, Cnr Main and Campground Roads, Newlands, Cape Town, 7700
P.O. Box 44911, Claremont, South Africa, 7735
Tel: +2721 657 4999 | Fax: +2721 657 4988
www.skybluefm.com

Source: Morningstar Direct

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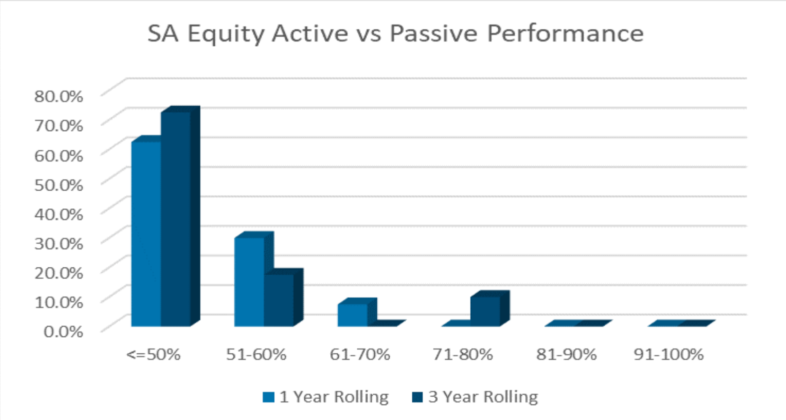
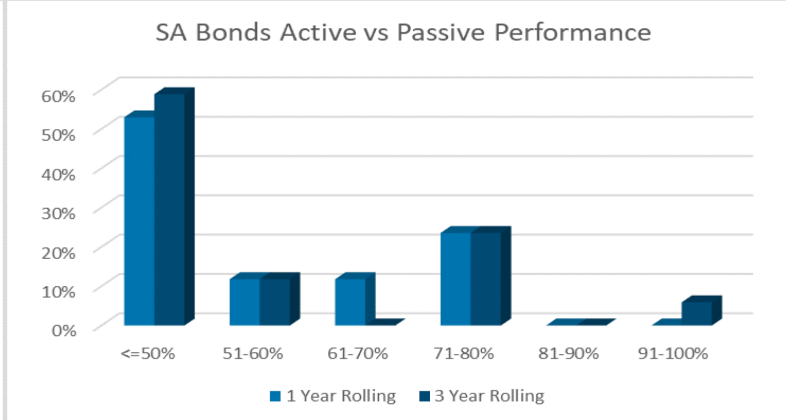
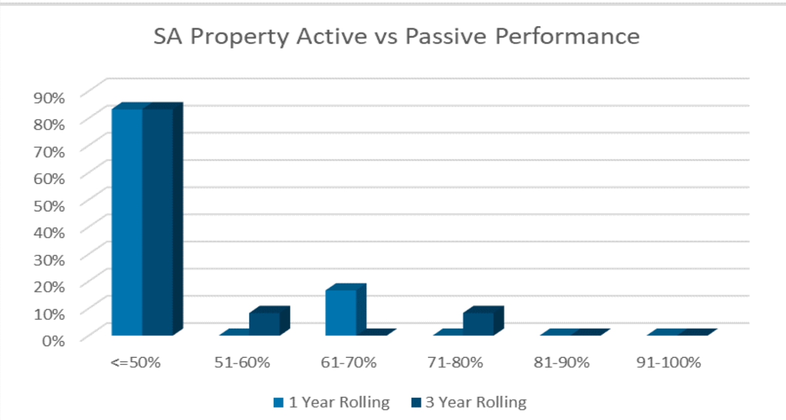
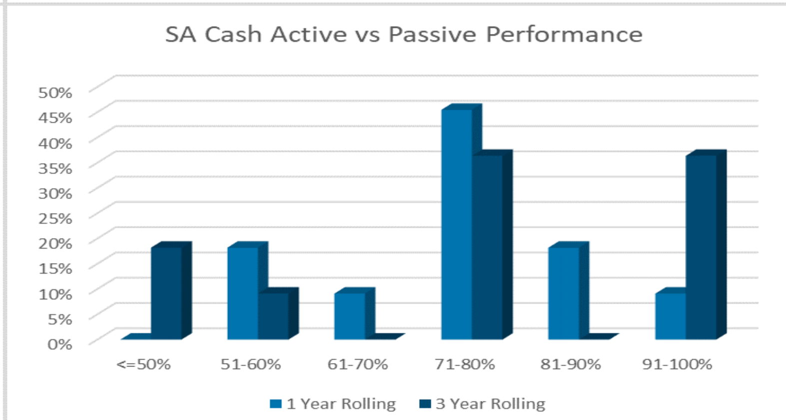
Some Food for Thought (cont.)



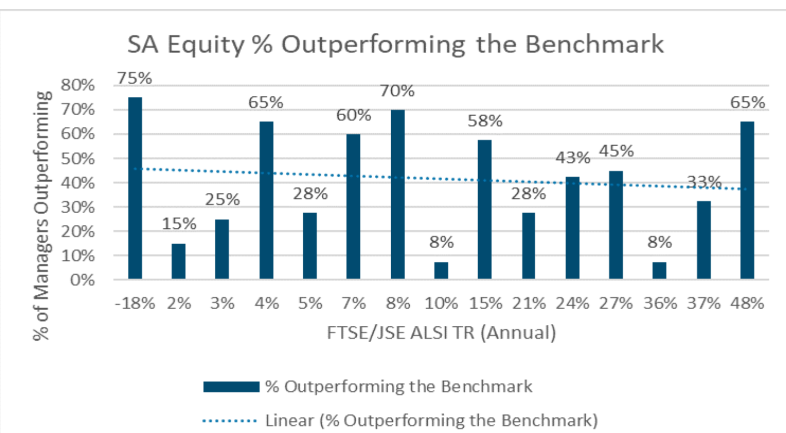


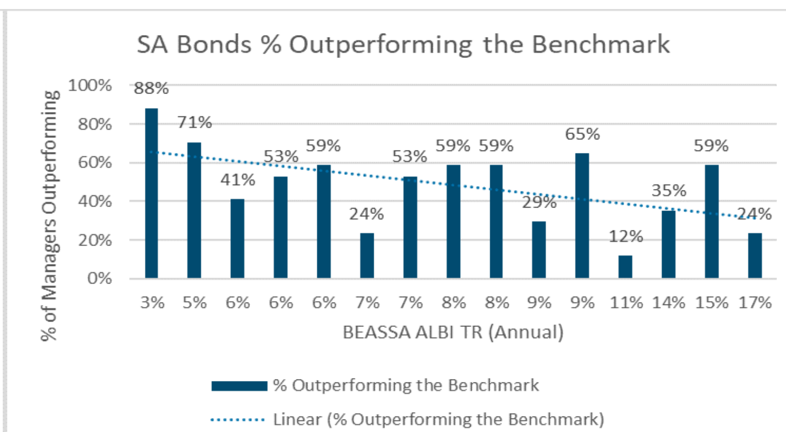




As can be seen, all the asset classes, except for Cash, are skewed to the left, indicating that the majority of active managers struggle to beat the return of the benchmarks on a consistent basis (or a high percentage of the times). The data does not suggest that all active managers underperform their benchmarks, but rather that the odds of selecting an active manager that will outperform the benchmark is extremely difficult. The cash or ASISA IB Short Term is the outlier in this test, it being skewed to the right, indicating that almost half of the active managers in this space have been able to outperform the Stefi Composite index 71% to 80% of the time over the last 15 years.

The focus of our study then shifted to the performance of active managers over different market conditions. For this, the study measured the total return of the index relative to the percentage of active managers that managed to outperform in that time period. The one calendar year rolling returns were used to measure the performance.





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P.O. Box 44911, Claremont, South Africa, 7735
Tel: +2721 657 4999 I Fax: +2721 657 4988
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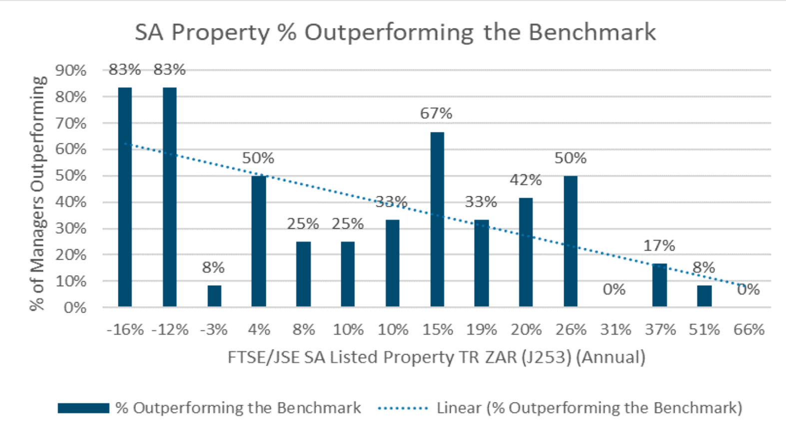

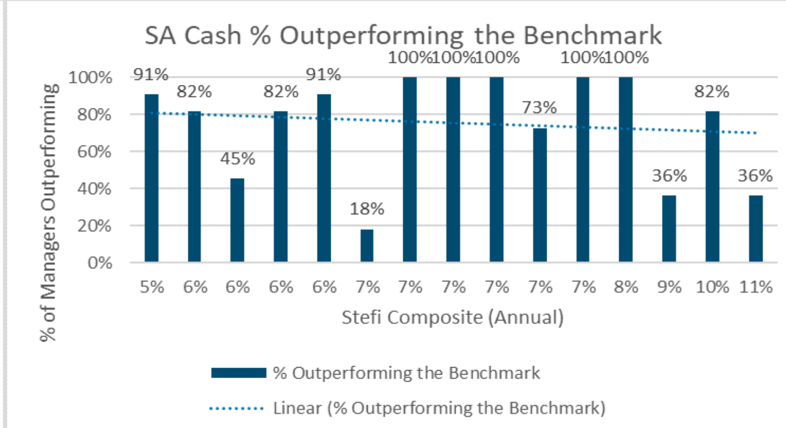

From the above it is evident that on average managers struggle to outperform the indices during strong bull markets, except for the active Cash manager who shows strong performance throughout the different market conditions. It is interesting to note however that the highest incidence of outperformance for local Equity, Bond and Property managers occurs during the most extreme bear markets, indicating that on average managers offer the best value during market downturns. This is to be expected as managers have the option to allocate toward cash, non-cyclical stock or lower the portfolio duration in the case of bond managers.

In summary, we believe that passive/index tracking investments have a place in the local Equity, Bond and Property space, especially as a core beta exposure. As for the Active Income/Cash asset class, we believe the active managers offer significant value and the data suggests that the odds are stacked in your favour for selecting a manager that will outperform the benchmark. That being said, it is not a clear cut answer as a niche manager can very successfully be used in conjunction with a passive investment as a satellite-core approach, or for protecting the asset class exposure on the downside during market downturns.

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P.O. Box 44911, Claremont, South Africa, 7735
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www.skybluefm.com

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Skyblue BCI Solar Flexible Fund of Funds

Global Multi Asset Flexible Allocation - More than 85% offshore

Proxy Benchmark: 60% MSCI World; 30% Barclays Global Bond Index; 10% US Cash

Fund Commentary

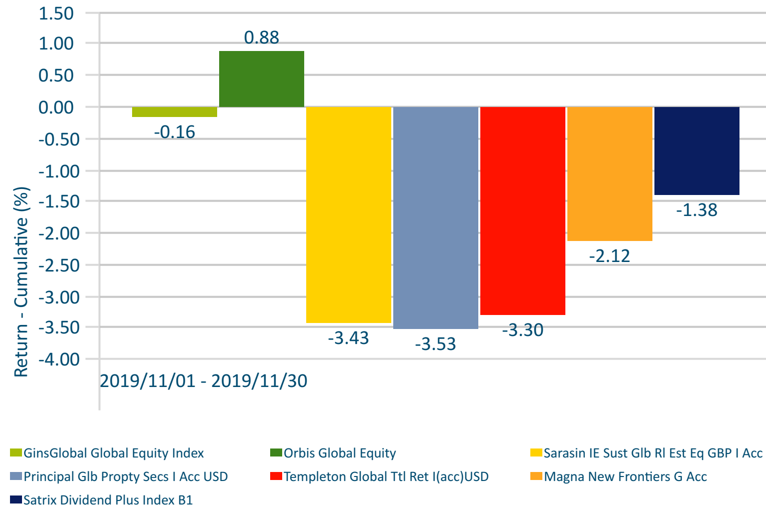
November was a good month for the South African Rand, which, it appears, is being supported by the global appetite for yield, leading to foreign investors piling in to our high real yields. The current low inflationary environment, combined with a hawkish South African Reserve Bank Monetary Policy stance, is creating very attractive real yields (bond yields net of inflation.) Current real yields are comparable to yields last seen 10 years ago and only a few times over the last 20 years. The Reserve Bank is being cautious given the ratings agencies' remarks, with their focus predominantly on supporting the currency so as to make foreign debt/interest payments more palatable in the event of a ratings downgrade.

Solar retreated 2.04% over the month on the back of the Rand strength discussed above. The best underlying performer was Orbis Global Equity adding 0.88% regardless of currency movements. The worst detractor was Principal Global Property, which was limited in extent given that exposure to global property was reduced substantially during the month.

The profit from global property sales was switched into longer term frontier market equity exposure. The fund is still diversified and is underweight global equity. Given the higher exposure to Frontier and South African markets it is considered imperative to have a buffer, which in our case is the global income exposure and broad diversification, in the event these holdings were to turn bearish. December tends to be a quiet period, given the festive season holidays, which can create some stability and even unveil some opportunities.

Underlying Holdings Return - November

Currency: South African Rand



Calendar Year Returns - Cumulative (%)

	1 Year	3 Year	5 Year	10 year
Skyblue BCI Solar Flexible FoF	11.56	20.99	52.01	154.75
(ASISA) Global MA Flexible (Sector)	16.47	27.20	54.84	196.43
Stefi + 5% (Benchmark)	12.68	43.30	80.46	206.40

Calendar Year Returns - Annualised (%)

	1 Year	3 Year	5 Year	10 year
Skyblue BCI Solar Flexible FoF	11.56	6.56	8.74	9.80
(ASISA) Global MA Flexible (Sector)	16.47	8.36	9.14	11.48
Stefi + 5% (Benchmark)	12.68	12.75	12.53	11.85

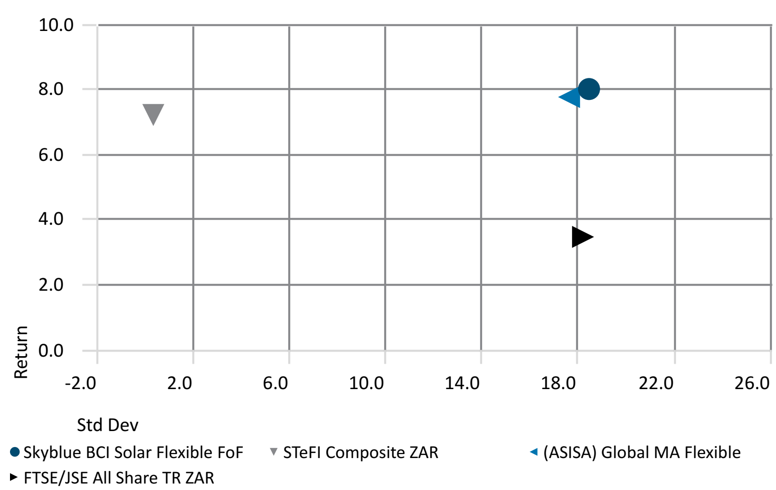
*Annualised return is the weighted average compound growth rate over the period measured.

Skyblue BCI Solar Flexible FoF - Monthly Returns

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2019	-1.90%	7.08%	2.75%	2.13%	-1.80%	-0.32%	1.42%	1.34%	2.01%	1.09%	-2.04%		
2018	-0.06%	-5.20%	-0.37%	6.68%	1.01%	5.68%	-1.44%	10.03%	-2.60%	-1.49%	-5.27%	-0.41%	5.51%
2017	-0.61%	-0.14%	2.84%	0.78%	-0.60%	0.02%	2.10%	-1.31%	4.82%	5.60%	-2.87%	-7.81%	2.14%
2016	1.52%	0.44%	-6.88%	-2.94%	10.81%	-7.14%	-1.87%	4.04%	-4.78%	-1.20%	3.13%	0.22%	-5.88%
2015	0.61%	2.81%	0.04%	2.33%	1.63%	-0.72%	3.17%	2.98%	3.34%	1.43%	4.18%	7.12%	32.80%
2014	-0.52%	2.77%	1.51%	1.09%	1.17%	1.42%	0.76%	-1.07%	-0.47%	-0.85%	1.71%	0.73%	8.49%
2013	5.14%	-1.61%	1.05%	-1.94%	7.81%	-6.23%	3.45%	1.08%	3.61%	2.88%	-0.78%	2.93%	17.94%
2012	4.95%	1.59%	-0.23%	1.41%	-2.56%	-0.16%	1.81%	2.50%	1.43%	3.34%	1.54%	0.90%	17.61%
2011	-0.32%	-0.94%	0.57%	1.65%	-0.04%	-2.42%	-1.17%	-2.57%	-0.91%	6.07%	0.60%	-1.03%	-0.78%
2010	-1.74%	0.52%	4.67%	0.62%	-3.96%	-0.66%	3.38%	-2.53%	4.90%	2.95%	0.39%	2.04%	10.64%
2009	1.54%	-4.36%	3.58%	2.58%	4.89%	-1.82%	5.79%	3.92%	0.57%	3.42%	0.98%	2.18%	25.39%
2008	-3.03%	2.54%	-0.74%	0.89%	1.76%	-1.44%	-4.34%	1.73%	-5.88%	-7.37%	0.06%	0.47%	-14.82%
2007											-2.01%	-1.22%	

Risk-Reward

Time Period: 2015/05/01 to 2019/11/30



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Source: Morningstar Direct

Skyblue BCI Cumulus Moderate Fund of Funds

South Africa Multi Asset High Equity Allocation - 0% - 75% South African Equities

Benchmark: Cash (SteFi) + 3%

Fund Commentary

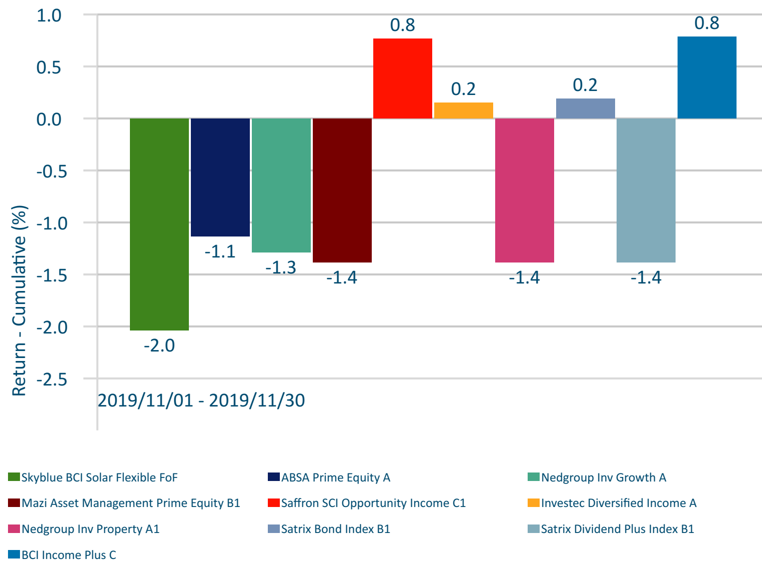
Cumulus pulled back 0.75% in November, as losses from the equity and offshore assets detracted significantly from performance. The income exposures, excluding long duration bonds, provided some stability however, making positive contributions for the month.

The best performing underlying funds for the month were the recently added BCI Income Plus, and Saffron SCI Opportunity Income, both delivering 0.8%. The worst performing underlying fund was Skyblue BCI Solar Flexible, posting negative 2%, on the back of Rand appreciation throughout the month and negative returns from the small exposure to local equity. Although our equity managers all protected some of the downside relative to the All Share index, absolute returns were still negative for November.

Our Strategic Asset Allocation models are still pointing to a risk on allocation environment, with valuations in the equity market favouring those over bond markets at current levels. Tactically our allocations remain overweight to high yielding fixed income instruments, albeit primarily in shorter duration instruments, where there are still very attractive risk-adjusted returns available. We remain cognisant of credit risk however, and therefore focus on high quality exposures and well-diversified portfolios within the short-term income space. We have a small tactical overweight to longer duration bonds as well, based on the high level of real yields available, low inflationary pressures, and continued pressure on the Reserve Bank to cut interest rates. There will however, likely be a period of higher volatility in this asset class as we approach the February budget and rating agency reviews.

We are not making many changes as we go into year-end. Uncertainty remains high, valuations depressed, and confidence at all-time lows. For now we remain diversified, tilted to short term income, but with healthy exposures to risky assets.

Underlying Holdings Return - November



Calendar Year Returns - Cumulative (%)

	1 Year	3 Year	5 Year	10 year
Skyblue BCI Cumulus Moderate FoF	3.06	4.97	19.91	114.79
(ASISA) South African MA High Equity (Sector)	8.86	15.58	26.04	124.81
Stefi + 3% (Benchmark)	10.53	35.27	63.92	152.81

Calendar Year Returns - Annualised (%)

	1 Year	3 Year	5 Year	10 year
Skyblue BCI Cumulus Moderate FoF	3.06	1.63	3.70	7.95
(ASISA) South African MA High Equity (Sector)	8.87	4.95	4.74	8.44
Stefi + 3% (Benchmark)	10.54	10.60	10.39	9.72

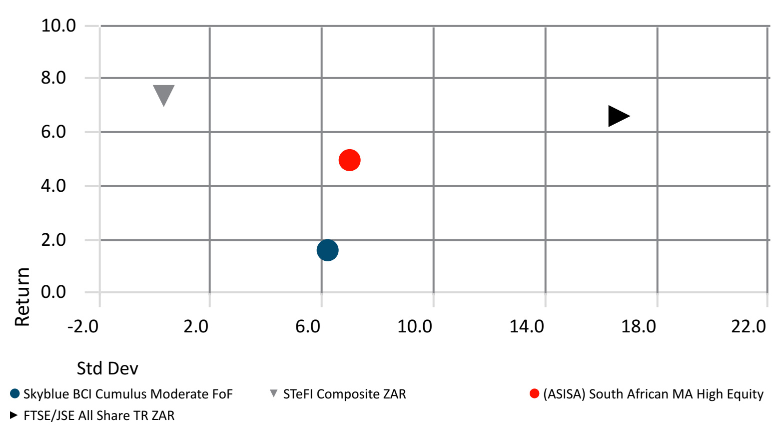
*Annualised return is the weighted average compound growth rate over the period measured.

Skyblue BCI Cumulus Moderate FoF - Monthly Returns

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2019	1.93%	1.22%	1.14%	2.16%	-2.32%	0.70%	-0.93%	-2.92%	0.62%	1.53%	-0.75%		
2018	0.32%	-0.62%	-1.78%	2.90%	-1.12%	1.27%	0.33%	3.55%	-2.67%	-3.28%	-2.73%	0.78%	-3.25%
2017	1.50%	-0.74%	1.53%	1.05%	0.06%	-2.42%	2.82%	0.64%	0.34%	3.48%	-0.51%	-2.45%	5.24%
2016	-1.36%	0.35%	1.78%	0.84%	2.87%	-2.07%	0.38%	1.41%	-0.69%	-1.55%	1.58%	0.82%	4.31%
2015	1.62%	2.23%	0.44%	1.48%	-0.46%	-0.56%	0.86%	-0.35%	0.22%	2.58%	-0.12%	0.94%	9.19%
2014	-0.26%	1.52%	1.46%	1.40%	0.84%	1.29%	0.47%	-0.99%	0.39%	-0.25%	1.32%	1.12%	8.59%
2013	5.39%	-0.30%	2.00%	-0.36%	6.83%	-3.87%	2.79%	1.47%	3.08%	2.05%	-0.52%	2.36%	22.51%
2012	2.87%	0.71%	0.45%	0.93%	-1.25%	0.65%	1.94%	2.87%	0.64%	2.47%	2.23%	1.01%	16.58%
2011	0.45%	0.19%	-0.22%	0.54%	1.07%	-1.03%	-0.52%	0.19%	0.34%	3.95%	0.79%	0.19%	6.05%
2010	0.28%	1.39%	1.56%	0.83%	-1.44%	-0.12%	1.74%	-0.33%	1.78%	1.26%	0.25%	1.25%	8.75%
2009	1.03%	-1.81%	2.41%	1.20%	1.22%	-0.46%	3.63%	2.00%	0.05%	2.63%	-0.32%	1.26%	13.48%
2008	-1.28%	2.27%	0.01%	0.22%	0.52%	-1.02%	-1.36%	2.04%	-1.54%	-2.51%	1.04%	0.22%	-1.50%
2007											-0.75%	-0.92%	

Risk-Reward

Time Period: 2016/12/01 to 2019/11/30



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THE ART OF INVESTING

Source: Morningstar Direct

Skyblue BCI Kimberlite Cautious Fund of Funds

South Africa Multi Asset Low Equity Allocation - 0% - 40% South African Equities

Benchmark: Cash (SteFi) + 1%

Fund Commentary

Kimberlite pulled back 0.36% in November, as losses from the equity and offshore assets detracted significantly from performance. The income exposures, excluding long duration bonds, provided some stability however, making positive contributions for the month.

The best performing underlying fund for the month was the recently added BCI Income Plus, delivering 0.8%. The worst performing underlying fund was Skyblue BCI Solar Flexible, posting negative 2%, on the back of Rand appreciation throughout the month and negative returns from the small exposure to local equity. Although our equity managers all protected some of the downside relative to the All Share index, absolute returns were still negative for November.

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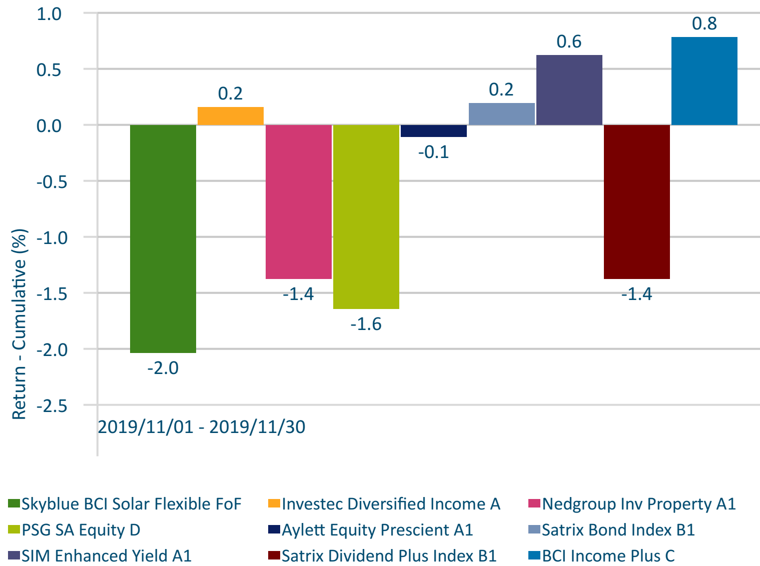
Underlying Holdings Return - November



Calendar Year Returns - Cumulative (%)

	1 Year	3 Year	5 Year	10 year
Skyblue BCI Kimberlite Cautious FoF	-0.17	4.54	18.02	89.29
(ASISA) South African MA Low Equity (Sector)	8.43	19.11	32.95	112.94
Stefi + 1% (Benchmark)	8.39	27.55	48.61	107.81

Calendar Year Returns - Annualised (%)

	1 Year	3 Year	5 Year	10 year
Skyblue BCI Kimberlite Cautious FoF	-0.17	1.49	3.37	6.59
(ASISA) South African MA Low Equity (Sector)	8.43	6.01	5.86	7.85
Stefi + 1% (Benchmark)	8.39	8.46	8.25	7.59

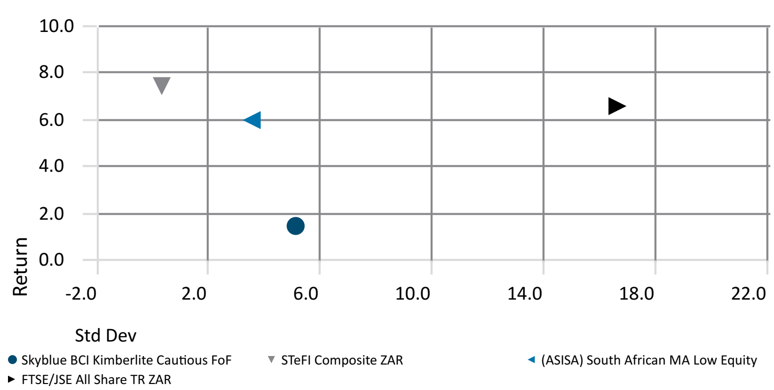
*Annualised return is the weighted average compound growth rate over the period measured.

Skyblue BCI Kimberlite Cautious FoF - Monthly Returns

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2019	1.50%	-0.10%	0.38%	1.49%	-1.42%	-0.20%	-0.31%	-2.53%	0.36%	0.92%	-0.36%		
2018	0.63%	0.01%	-1.03%	2.04%	-0.72%	0.82%	0.46%	2.98%	-1.82%	-1.47%	-2.78%	0.17%	-0.85%
2017	0.93%	-0.20%	1.15%	0.46%	-0.27%	-1.30%	1.96%	0.45%	0.99%	2.37%	-0.57%	-1.12%	4.86%
2016	-0.61%	0.49%	1.74%	0.99%	1.84%	-0.99%	0.61%	1.10%	-0.14%	-0.94%	1.73%	0.89%	6.85%
2015	0.78%	1.26%	0.01%	1.10%	-0.27%	-0.68%	0.71%	-0.64%	-0.07%	2.08%	-0.24%	0.98%	5.11%
2014	0.34%	0.15%	1.18%	1.33%	0.48%	1.12%	0.43%	-0.80%	-0.23%	-0.64%	1.02%	1.42%	5.94%
2013	3.70%	0.64%	1.96%	1.05%	1.89%	-1.47%	1.06%	-0.05%	2.03%	1.09%	-0.13%	1.74%	14.28%
2012	1.51%	0.55%	0.87%	0.66%	-0.14%	0.72%	1.76%	2.42%	0.04%	1.28%	1.81%	1.10%	13.31%
2011	0.33%	0.09%	0.01%	1.13%	0.95%	-0.56%	-0.21%	0.62%	1.34%	2.24%	1.14%	0.18%	7.49%
2010	1.10%	1.26%	1.15%	0.77%	-1.55%	0.28%	2.00%	-0.29%	1.91%	0.88%	0.21%	1.11%	9.15%
2009	0.91%	-1.30%	2.50%	1.33%	0.83%	-0.68%	2.99%	0.93%	-0.41%	2.34%	-0.75%	1.08%	10.11%
2008	0.22%	1.81%	0.72%	-0.47%	0.32%	-0.31%	0.57%	2.02%	-0.38%	-1.50%	1.82%	0.18%	5.05%
2007											-0.21%	-0.26%	

Risk-Reward

Time Period: 2016/12/01 to 2019/11/30



Skyblue Fund Managers (Pty) Ltd.
7th Floor, Letterstedt House, Cnr Main and Campground Roads, Newlands, Cape Town, 7700
P.O. Box 44911, Claremont, South Africa, 7735
Tel: +2721 657 4999 I Fax: +2721 657 4988
www.skybluefm.com

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Source: Morningstar Direct