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UP

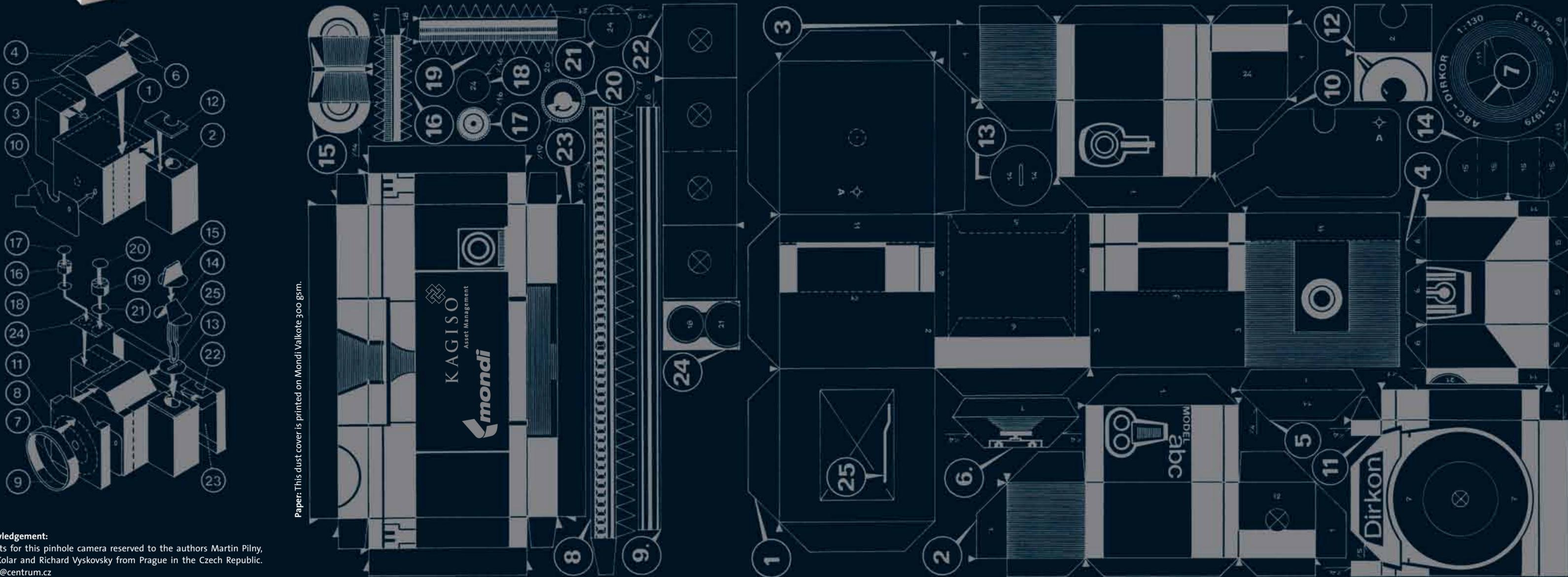
January 2011
Kagiso Asset Management
Quarterly newsletter

Instructions: This is a Czech Republic translation of the original Dirkon instructions printed in 1979

Who isn't familiar with the pinhole camera, the predecessor of today's modern camera? You would certainly have heard about it at some point. Today you can have a go at making it and experiment to see how it was used to "capture images" in the past. The principle is the same, except that it requires modern film. You need to get a classic 35mm film. The best film to use in this case is Foma 21° DIN. Higher sensitivity will enable a short exposure. After you have stuck the various parts of the camera together and let it dry properly, insert a filmroll containing film into the right-hand small side box (viewed from the back). Pull out the film approximately 6-8 cm and insert the end into the other reel - a second, empty film roll. You can get these in any photolab. Turn the "key" on the empty cassette (section 15) so that the marker on the key goes through $360^\circ + 180^\circ$, i. e. three half-turns. You make your exposure by moving the shutter (10) down and up, thus opening and closing the "lens". You have to play around with the exposure to get it right. With Foma 21 film, it's about 1 second on a really sunny day. Naturally, you have to place the camera on a firm base and it mustn't be moved at all when handling the shutter.

And now for the instructions on how to put the camera together: First you take an office paper clip and bend it as indicated in the drawing (25). Then you make cutouts in sections 1, 2, 7, 11, 13 and 24. Now take part 10 and, using a press stud (popper), fix it to your completed section 1 at point A, where you make a tiny hole with a small nail. Put section 1 together and attach the small side boxes (sections 2, 3), which will have been made beforehand. These boxes serve as containers for the film rolls. Stick section 12 together and attach it to section 2. Then section 24 to 3. From sections 4, 5 and 6 make a fake viewfinder for the top and place it onto the main section 1. "Lens": attach the outer part 8 to section 7 and stick it together from inside with section 9; then stick this whole section to the front of 11. Now stick the whole "lens" to the camera. TAKE CARE only to stick down the side, lower and upper flaps and make sure that the shutter can move freely in the space between the camera and the front cover with its "lens". Before putting on the cover at the end, check that the press stud (popper) fastening is secure. Now work on the additional parts using the drawing as a guide: make the fake buttons from sections 16, 17, 18 and 19, 20, 21 (these aren't operational); fix these onto 24. Stick the bent paper clip (see 25) to the middle of section 14 and cover it with section 15. Slide on part 13 from underneath and attach it to section 14. This gives you the key for winding the film. Finish this part off with the folded section 22, which, when inserted above the film roll, prevents light from coming in. Slide the key from above through folded section 22 into the slot in the film reel. Carefully construct the back section 23 by folding the edges (reinforced border). Line the inside of the back wall with thin black velvet (from any haberdasher's). The velvet acts as lightproof protection and keeps the film level inside the camera - an essential feature! You can protect the camera from opening at the wrong time by putting two black rubber bands over the entire body of the camera.

NOW BE CAREFUL! This is an important operation which depends on accuracy! Pull the shutter down to reveal the little disc drawn on section 1, with the little dot in the middle. Take a needle of diameter 0.4 mm (this must be exact) and pierce the dot cleanly. Only do it once, don't try and repeat the procedure! The sharper the pinhole, the cleaner and sharper the image. If you go wrong, cover up the hole with a piece of thin card and have another go. And now all you do is wait for the sun and then you can go out and take photographs. Dirkon creators Martin Pilny, Mirek Kolar and Richard Vyskovsky wish you good light and great pictures, which will naturally have a softer outline than ordinary photographs.



Paper: This dust cover is printed on Mondi Valkote 300 gsm.

Acknowledgement:

All rights for this pinhole camera reserved to the authors Martin Pilny, Mirek Kolar and Richard Vyskovsky from Prague in the Czech Republic. m.pilny@centrum.cz

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Dirkon: The innovative paper cut-out camera. The images used in this newsletter were taken with a pinhole camera made out of Mondi paper. The template on the dust cover originates from the Dirkon camera, which was first published in 1979 in Communist Czechoslovakia, in the magazine “ABC Mladych Techniku a Prirodovedcu” (“An ABC of Young Technicians and Natural Scientists”). Its creators, Martin Pilny, Mirek Kolar and Richard Vyskovsky, invented a functional pinhole camera made of stiff paper, designed for 35 mm film. The Dirkon resembles a real camera. Amazingly, as seen in this newsletter, it works.

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Cover image of paper reels taken at Mondi warehouse, Montague Gardens

Dirkon setting: Fifteen second exposure on 100 ASA colour positive film. Digital SLR setting: One second exposure @f22, 100 ASA.

----- Unconventional thinking. Superior performance -----



Dirkon setting: Three second exposure on 100 ASA colour negative film. Digital SLR setting: One fifth of a second exposure @f22, 100 ASA.

Why we believe we'll continue to outperform

Roland Greaver - Chief Executive Officer

Over the years, performance trends in relative asset classes in financial markets and innovations in types of instruments and strategies have shaped business models in the asset management industry.

The lower real returns in developed markets in the early 1980's saw the emergence of higher-yielding, riskier asset classes such as private equity and high yielding debt instruments.

Another major shift of the 1980's was from balanced funds to specialist funds in order to achieve higher returns through specialist portfolio construction.

Why we believe we'll continue to outperform

Globally, the hedge fund industry gained prominence in the mid-1990's in response to higher volatility in mainstream asset classes, while the financial crisis of 2008/2009 had its origins in the demand for ever higher yielding, more exotic debt instruments.

Product proliferation

The traditional response by asset managers to these trends in relative performance and financial market innovation is to launch new products and to attempt to protect, grow and diversify revenue streams. This results in product proliferation and multiple styles and strategies housed in a single investment manager.

Evidence seems to suggest that following new trends is not often in the client's best interests. New products offered may not provide real long-term investment benefits to clients (specialist IT sector funds launched in the late 1990's, US high yield debt funds in the 2000's). New products may not be backed by true competence in the particular investment manager and this is hard for the client to identify. Additionally, resultant wide product offerings within an investment manager may diminish levels of focus and create internal tensions - detracting from existing areas of competence.

Circle of competence

At Kagiso Asset Management we believe in excelling in a limited number of areas, within which we operate with high conviction. We operate within our circle of competence and only in areas where we believe we can consistently excel. Our product range is concentrated in specialist asset class funds and asset allocation funds, which are complementary and clearly differentiated by expected risk and return characteristics. Most importantly, our different fund strategies are designed to meet enduring needs of different types of clients.

Matching portfolio size to scalability of strategy

We are convinced that many investment strategies are less effective above a certain portfolio asset size - that is: the ability of the investment manager to outperform reduces when funds deployed in the same strategy become too large. There are many reasons for this in the South African context, including that, with increasing fund size:

- ◆ Fewer different investment options exist, i.e. lower breadth, resulting in lower portfolio diversification and lower ability to differentiate the portfolio from competitor funds and "the market". Large manager portfolios are inevitably similar to each other and have higher risk.
- ◆ Large managers are constrained mainly to large investment issues, e.g. large capitalisation companies for equity managers. When large managers invest meaningfully in smaller issues, they are forced to hold long-term strategic stakes that are more or less permanent.
- ◆ Liquidity is constrained, as very large portfolio positions are very difficult to trade into, and out of, as the relative investment attractiveness changes.

Our sense is that the above considerations are particularly pertinent to the highly concentrated South African listed equity market (an area of specialisation for Kagiso Asset Management) - perhaps more so than is conventionally appreciated. Other areas where there appear to be size constraints on portfolios in South Africa are: private equity, corporate bonds, listed property and most hedge fund strategies.

At Kagiso Asset Management we will always endeavour to constrain our total portfolio asset size in any strategy or asset class at a level, beyond which we believe our performance advantage over the competition starts deteriorating.

"We believe in excelling in a limited number of areas, within which we operate with high conviction."

Effectively deploying the best investment talent with a proven investment philosophy

Most importantly, our ability to continue to outperform for clients derives from our future success in attracting, retaining, developing and incentivising the best investment talent available in the market. These investment professionals must be able to operate within an unconstrained environment, where they are not distracted from their investment research and decision-making by bureaucracy or institutional demands on their time.

They need to operate with conviction in executing our proven investment philosophy, free from distractions and encouraged to think deeply and unconventionally.

We believe that the environment that is essential for long-term success for clients is only truly possible to maintain in an owner-managed, autonomous, medium-sized investment manager that passionately preserves the appropriate professional culture and is able to reward exceptional, differentiated thinking.

2010 milestones for Kagiso Asset Management

- ◆ We reached R28 billion as at 31 December 2010 in assets under management, following strong growth in assets from new clients, meaningful flows from existing clients and strong equity market performance.
- ◆ We maintained our position as number one fund in the General Equity unit trust sector since the inception of the Equity Alpha Fund in April 2004.

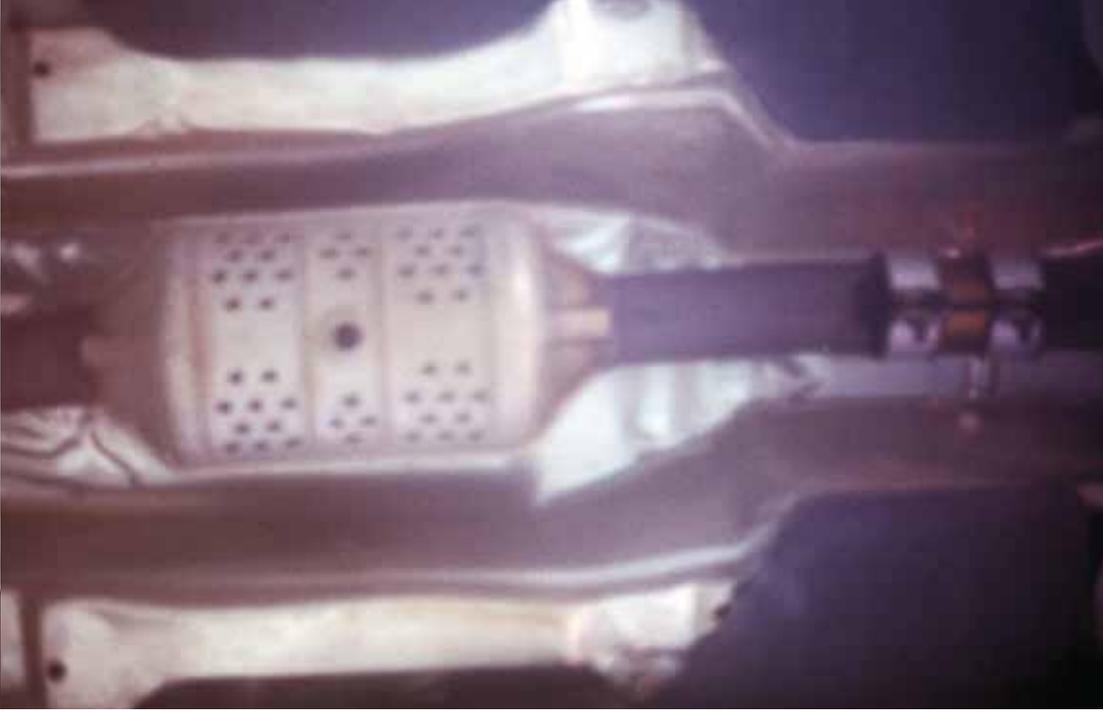
“We believe the environment that is essential for long-term success for clients is only truly possible to maintain in an owner-managed, autonomous, medium-sized investment manager.”

- ◆ We gained access to a number of LISP platforms, thereby strongly developing the ability for new clients to access our unit trust funds.
- ◆ We gained a number of new clients in our fast-growing asset allocation funds.
- ◆ We substantially developed our internal IT systems, our compliance function and our operational capacity.
- ◆ We launched our own unit trust management company, which brought to an end an association of nine years with Coronation Fund Managers. Up until then, Coronation managed the back office and client communication function of our retail funds.

As a result of this last development, you will be receiving this new investment newsletter on a quarterly basis. We trust that the first issue of UP will be a stimulating and insightful read.

Thank you for your continued support and wishing you everything of the best for 2011.

Roland Greaver - Chief Executive Officer



Dirkon setting: Forty second exposure on 100 ASA colour positive film. Digital SLR setting: Five second exposure @f22, 100 ASA.

The World of Platinum Group Metals

Abdul Davids - Head of Research

South Africa occupies a unique place in the Platinum Group Metals (PGMs) landscape: close on 85% of the world's known PGMs are located at the Bushveld Igneous Complex, covering an area of around 65 000km² (see chart on following page).

The Bushveld Complex was formed by continuous injections of magma into a massive underground area or chamber, possibly caused by a giant meteorite strike. Simplistically, this magma cooled and crystallized over millions of years, forming a layered deposit as different minerals crystallized at different temperatures during the cooling process.

PGM reef types

Subsequent intrusions repeated the crystallization sequence and, through this process, similar minerals were deposited together. The PGMs (platinum - Pt, palladium - Pd, rhodium - Rh, ruthenium - Ru, iridium - Ir and osmium - Os) formed in two principal layers: the Merensky (named after pioneering geologist Dr Hans Merensky) and the Upper Group Chromitite number 2 (UG2) reefs. These reefs also contain high quantities of gold, nickel, copper and chrome.

The Merensky and UG2 reefs are believed to have formed across the underground

chamber and, over time, the edges of the Bushveld Complex have been moved towards the earth's surface, creating a saucer-like formation. The reefs can be identified for up to 300 km along two arcs or outcrops on the eastern and western limbs of the Bushveld Complex. They descend from the surface at an average dip of approximately 9° to 18°. The shallow outcrops are the primary target for PGM mining operations in the region.

In general, the geology of the Merensky reef makes it more difficult to mine than the UG2 reef as it is more prone to disruptions from faulting (particularly in the north-western

limb) and dilution from rolling reef. As a result, the Merensky reef is usually mined using handheld drills to allow greater flexibility and to prevent removal of unnecessary waste rock. The average cut applied is usually between 120 cm and 150 cm.

In contrast, the UG2 reef is relatively uniform and allows for greater use of mechanised equipment (particularly on the eastern limb). This is more cost effective, despite the larger cut

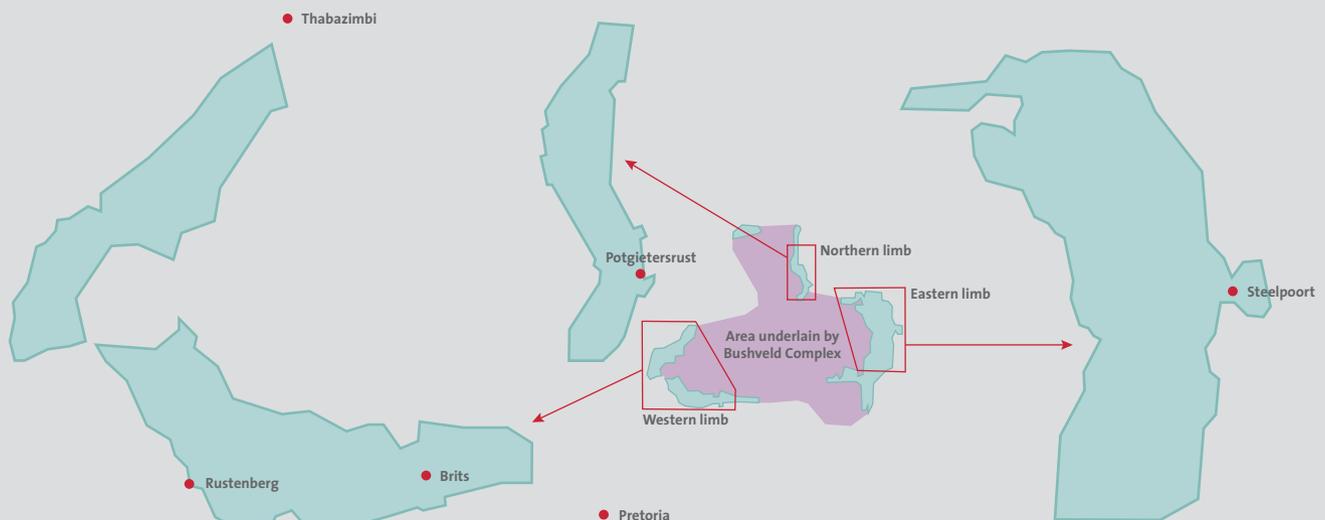
(180 cm to 220 cm) requiring more rock to be mined. On the negative side, the UG2 reef typically has higher chrome content than the Merensky reef. Chrome in the ore negatively affects

concentrator recoveries and can build up within the furnace, necessitating lengthy downtime for removal.

A third platinum-bearing deposit is also mined towards the north of the Bushveld Complex and is known as the Platreef. The Platreef is similar in formation to the Merensky reef, although the ore-body itself is thicker and not as easily defined. Compared to the rest of the Bushveld Complex, the Platreef is relatively rich in base metals (copper and nickel) and, given its thickness of approximately 20 metres, is very suitable for open cast mining.

“The PGMs formed in two principal layers: the Merensky and the Upper Group Chromitite number 2 (UG2) reefs.”

The Platinum Group Metals landscape



General map of the Bushveld Complex (centre)

Source: South African Journal of Science 95, November/December 1999

The World of Platinum Group Metals

Interestingly, rock temperatures increase faster as you descend in a platinum mine than in a gold mine. Rock temperatures of the world's deepest platinum mine, Northam's Zondereinde mine, can reach 75° C at depths of 2 500 metres. A typical gold mine in Gauteng's Rand area will reach this temperature at around five kilometres. This is relevant because the cost of cooling the working face, miners and equipment at such depths can be a significant negative feature and can prevent deeper mining.

The mining and concentrating process

The mining process for the various ore bodies differ because of differences in their respective geologies. Both the Merensky and UG2 reefs are very narrow - typically less than a metre thick. Historically, both reefs were mined using narrow reef methods and many operations continue to use these methods today. Miners use hand-held drills to bore holes, which are then filled with explosives. After blasting, ore is removed from the stope using scrapers attached to winches. It is then transported through a series of ore passes or shutes to the bottom of the shaft and hauled to the surface.

Above ground, the ore is crushed and milled to reduce the size of the rock particles and to expose the PGM minerals. Using a flotation process, the particles are mixed with water and special reagents and air is pumped through the liquid. This creates bubbles, to which the PGMs attach. These float to the surface and are removed as a soapy froth. The PGM content of this flotation concentrate varies between 100 and 1 000 grams per ton.

After being dried, the concentrate is smelted in an electric furnace at temperatures which can exceed 1 500° C. During this process, a matte containing the valuable metals is separated from the unwanted minerals, which form a slag and are discarded. The matte is transferred to converters, where air is blown through the matte in order to remove iron and sulphur. The PGMs content of the "converter matte" now exceeds 1 400 grams per ton.

Refining

The next step is to separate the base metals from the PGMs. The soluble metals - gold, palladium and platinum, which dissolve in hydrochloric acid and chlorine gas - are generally

the first to be extracted. The insoluble PGMs come out next, with rhodium usually last. The refined PGMs have a purity of over 99.95% and can be produced in a number of forms: ingot, grain or a fine powder known as

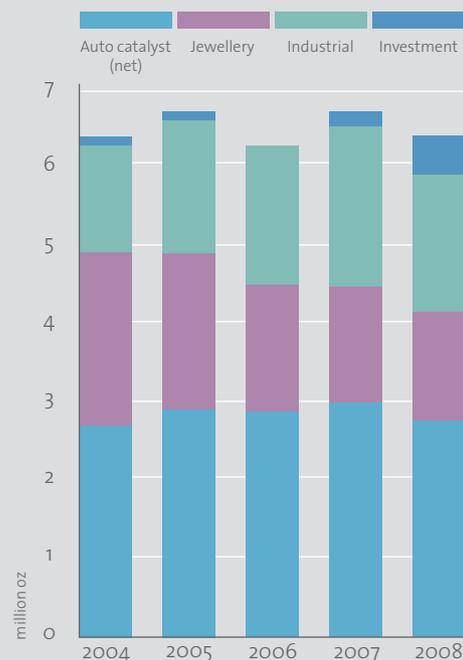
"sponge". The time between mining of the ore and production of pure metal typically ranges from around six weeks for palladium to up to 20 weeks for rhodium.

Demand for PGMs

Around 45% of all platinum produced is used in the automobile sector to manufacture catalytic converters for cars (auto catalysts). A further 30% is used for jewellery and around 25% is used for industrial purposes. Platinum demand has grown from around four million ounces in 1994 to 6.7 million ounces

"Around 45% of all platinum produced is used in the automobile sector to manufacture catalytic converters for cars."

Demand for platinum 2004 - 2008



Source: Johnson Matthey

in 2007 - a 4% growth rate per annum. Following the financial crisis and the concomitant global recession, demand has slipped back to around six million ounces. Demand is forecast to grow by 4.2% per annum to seven million ounces in 2012.

A key feature of the last five years has been the emergence of investment demand in the form of exchange traded funds (ETF's) in the platinum market. The growth in ETF's has contributed to the platinum price reaching a record high in 2008.

“When looking at demand for PGMs, a key feature of the last five years has been the emergence of investment demand in the form of exchange traded funds in the platinum market.”

Between 2007 to 2008, PGM prices rose to record highs as electricity outages severely curtailed PGM production and international buyers of PGMs frantically attempted to stockpile to avoid further price increases.

The table on the previous page highlights the changing dynamics in platinum demand and the emergence of investment demand through ETF's.

Setting a “normal” basket price

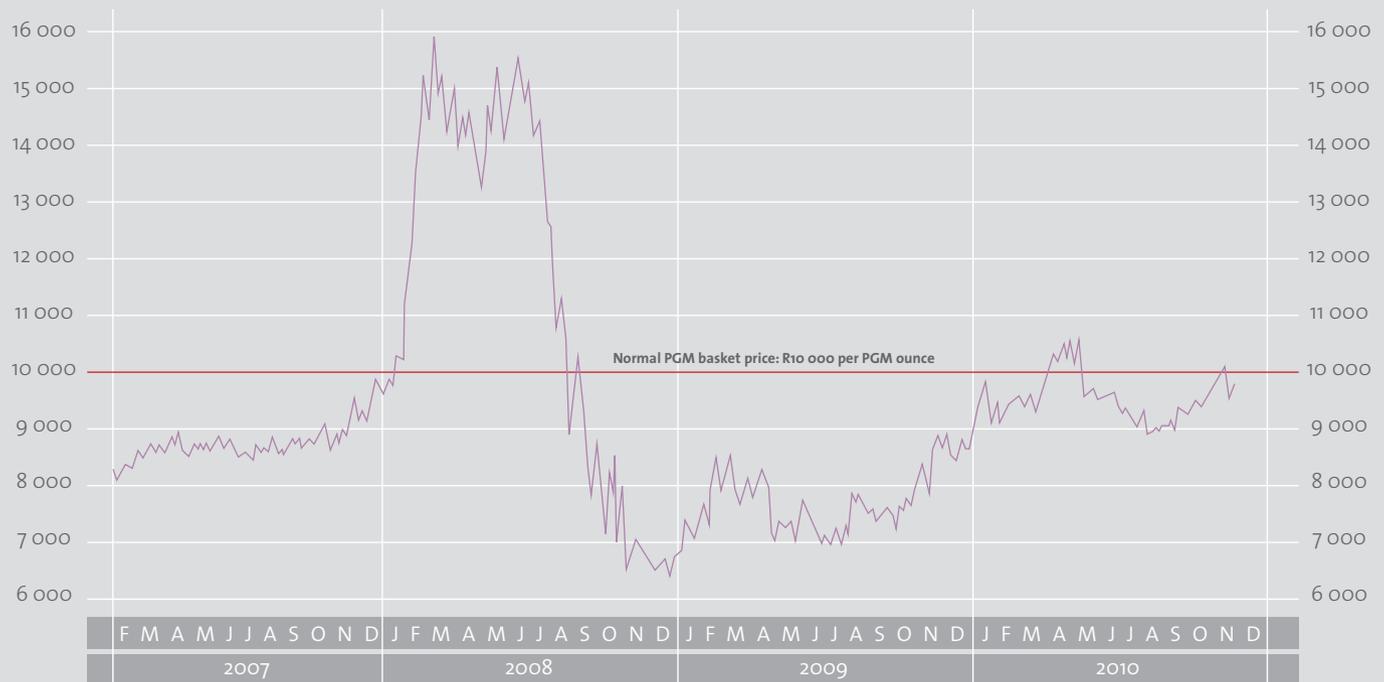
The PGMs occur in fairly uniform ratios across the Bushveld Complex. The PGM producers therefore have similar quantities of platinum, palladium, rhodium and other PGMs per ton of ore

at the end of the mining, smelting and refining process. The PGM producers’ revenues therefore comprise the ratio of the various PGMs (roughly 60% platinum, 30% palladium, 5% rhodium and 5% other) multiplied by the respective metal prices.

The July 2008 credit crisis, together with improved electricity management in South Africa, quickly restored an element of normality to the PGM market.

At current levels of demand and supply, the global PGM market is largely in balance, with both the platinum and palladium market relying on increased recycling to meet increased demand. Johnson Matthey, the global authority on the PGMs market, is forecasting a price range of between

The PGM basket price in rands



— PGM basket price R/oz (9787.25538)

Source: INet/Kagiso Asset Management research

The World of Platinum Group Metals

\$1 550 and \$1 900 per ounce for platinum.

The PGM market is forecast to run into a small deficit in 2011 as demand rebounds and supply remains constrained. Kagiso Asset Management has used a “normal” platinum price of \$1 550 and derived prices for the other metals as follows: palladium \$500, rhodium \$2 000 and gold \$950. Using an exchange rate R8 to the US dollar, the above prices translate into a “normal” rand basket price of R10 000 per PGM ounce.

Market shares

The chart below highlights the South African producers' dominance of world supply and resources.

Anglo Platinum is the world's biggest producer of PGMs and also controls the biggest share of known PGM resources. The South African platinum producers accounted for 76% of the world's PGM supply in 2009 (excluding supply from recycling).

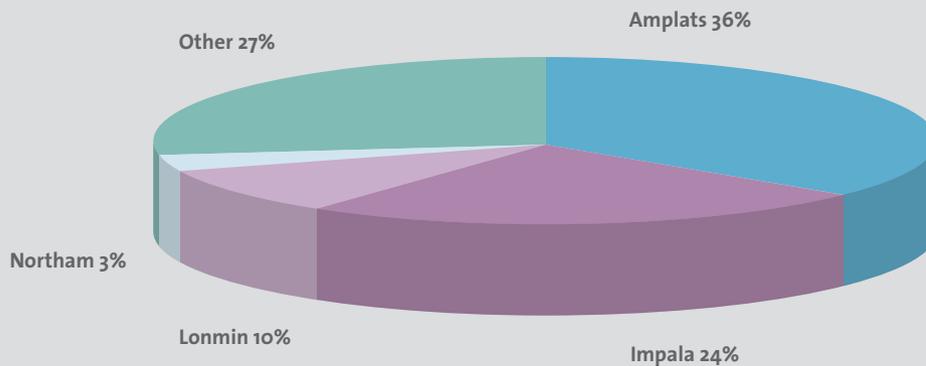
Conclusion

South Africa's unique geographic advantage makes the country a very important component in the global PGM market.

Any threat to the country's ability to produce PGMs, as seen in 2008, will result in an almost immediate impact on prices, demonstrating the country's pricing power in the market.

Kagiso Asset Management is therefore of the firm view that the South African PGM producers have an inherent competitive advantage relative to other mining companies and other industries and should therefore attract a premium rating relative to the South African equity market.

Platinum production (2009 - 6.9m oz)





Dirkon setting: One minute exposure on 200 ASA colour negative film. Digital SLR setting: One second exposure @f22, 200 ASA.

Mondi: Focused on emerging market growth

Rubin Renecke - Equity Analyst

International paper and packaging group Mondi is a significant holding in our clients' portfolios as we believe it is currently trading at a substantial discount to its intrinsic value.

Mondi has operations across 31 countries and is one of the lowest cost paper and packaging producers in the world due to its high levels of integration in wood and pulp. It is attractively positioned to deliver significant cash flows to shareholders after restructuring to focus strongly on emerging markets.

Mondi: Focused on emerging market growth

Mondi has, over the last five years, actively invested in its capital base by refurbishing existing assets to improve efficiencies and productivity. It has moved high cost capacity in its packaging operations out of countries like the UK, France and Italy into low cost production areas, where there is demand in domestic markets as well as the ability to export into Western Europe from a cheaper production base.

Industry background

Traditionally paper companies had a track record of over-investing in capacity. In addition to this, the advent of the Internet and other digital media over the last decade has caused a structural decline in paper demand in the developed world. This has caused excess supply of paper relative to demand and consequently downward pressure on paper pricing. Paper producers have therefore yielded very poor returns on shareholder capital, especially in the case of the higher cost producers.

Demand for coated paper, which is used for glossy magazines and advertising-type products, has declined the fastest. Mondi management took a strategic decision about 10 years ago to position itself in uncoated paper as well as in packaging production. Uncoated paper is mainly used in office printers and is geared towards desktop computer penetration. Packaging paper is predominantly for consumer products and is dependent on GDP growth to drive demand.

While, in developed markets, computer penetration is mature and demand for uncoated paper is stagnant to slightly declining, in faster growing emerging markets, such as Russia and Poland, personal computer penetration is still increasing. Demand for uncoated paper in these countries therefore continues to grow. In packaging paper, Mondi is more geared towards GDP growth in emerging markets following its relocation of production into Eastern Europe. In addition, in developed markets, environmental concerns are causing a move from non-recyclable plastic to recyclable paper packaging.

Integrated value chain

Wood is the primary raw material in paper production. Mondi operates 2.06 million hectares of forests in Russia and 332 000 hectares in South Africa. Mondi converts wood from forests into pulp and then into paper and packaging products. Mondi is about 60% self-sufficient in terms of wood and about 92%

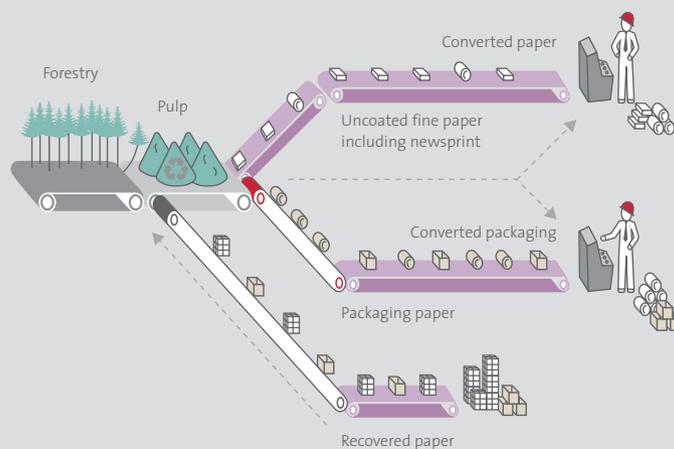
self-sufficient with respect to pulp (see diagram below).

The benefits for Mondi of being so highly self-sufficient, relative to competitors who must source pulp from external parties, are:

- ◆ A steady and predictable availability of pulp
- ◆ An ability to locate production facilities at or near forests and pulp production facilities with massive consequent savings (transport and logistics costs)
- ◆ Mondi is shielded from the cyclical volatility in the price of pulp

“Mondi management took a strategic decision about 10 years ago to position itself in uncoated paper.”

Mondi: Integrated value chain



Source: Mondi

Low cost operations

In the last five years, most of Mondi's investments have been made in emerging markets. A total of 64% of its expansionary capital expenditure was spent in emerging Europe between 2004 and 2009, while 29% was spent in South Africa. This, combined with recent expansions in Russia and Poland, is further entrenching Mondi's position at the low end of the cost curve. Its forestry operations in South Africa and Russia have amongst the cheapest wood production costs globally. The group's low cost integrated strategy allows it to survive tough times, when pricing is under pressure, and to gain market share. The diagram below shows its recent moves of packaging production from high cost to low cost areas.

A good example of the increasing contribution from low cost operations can be found in Swiecie, the Polish operation, which houses one of Mondi's material recent expansions. In 2004, Swiecie's contribution to group container board production was roughly 27%, increasing to just over 50% in 2009. This is expected to rise above 60% in 2010. Mondi's new paper machine at Swiecie is one of the lowest cost in the industry.

“Overall, Mondi has positioned itself as a leading low cost supplier of paper packaging products.”

Investment concerns

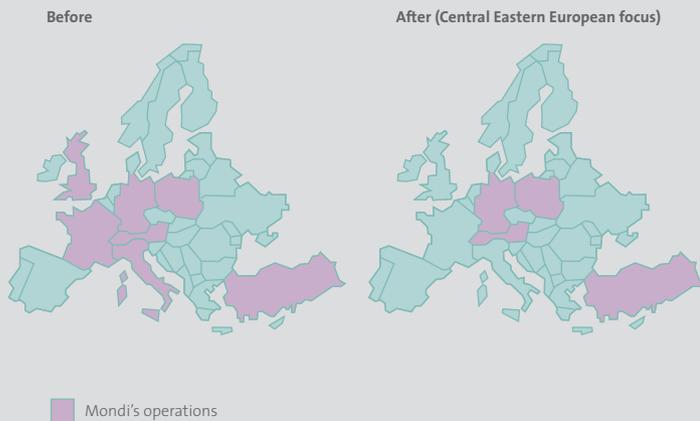
In our view, the biggest risk currently for Mondi is the prospect of a slowdown in global GDP growth, which will result in reduced demand for the group's paper and packaging products as well as pricing pressure. Raw material cost pressures and continued strong emerging market currencies are additional

challenges that Mondi has to contend with. These risks are offset by relatively low capital expenditure requirements in future as the bulk of Mondi's capital expenditure spend is now complete, shown in the chart below.

Strongly positioned in a tough market

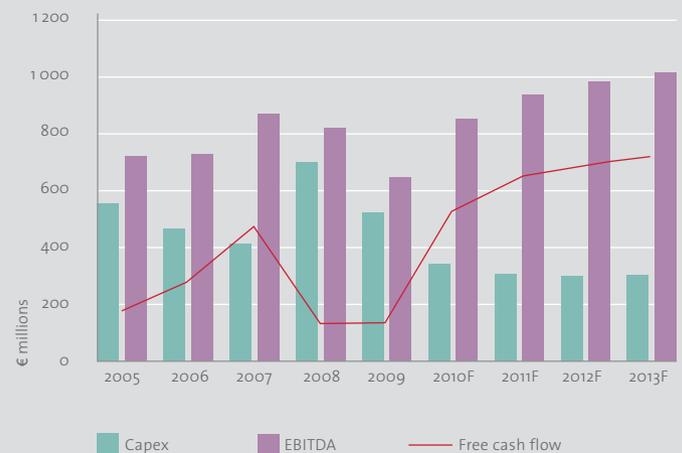
Overall, Mondi has positioned itself as a leading low cost supplier of paper and packaging products. We believe that this strategy, together with the fact that the group's major capital expenditure is complete, should enable the business to deliver a robust performance going forward as well as increased cash returns to shareholders despite current tough market conditions.

Mondi: Restructuring of packaging operations



Source: Mondi

Capex versus free cash flow



Source: Kagiso Asset Management research, company reports



Dirkon setting: Three second exposure on 100 ASA colour negative film. Digital SLR setting: One eighth of a second exposure @f22, 100 ASA.

Stimulus addiction and withdrawal

Gavin Wood - Chief Investment Officer

We end the first decade of the 21st century with markets booming, having recovered strongly from the great meltdown that (perhaps coincidentally) followed the Beijing Olympics in 2008.

Our sense is that the recent economic tumult has left us with an imbalanced world with below par growth prospects. Markets, however, seem to be addicted to powerful doses of stimulants of the fiscal and monetary kind and move ever higher after each “fix”.

Our clients’ portfolios remain defensively positioned as we worry that the symptoms from stimulus withdrawal may be severe.

Looking back

As can be seen from the table below, the past decade has seen tremendous volatility and has ended with some new extreme highs, yet some prices hardly moved (US equities and the rand).

In the lead-up to the 2008 crisis, the global economy had been unsustainably buoyed by significant private sector stimulus.

Developed market banks, poorly managing risk, exploited the false notion that house prices always rise and that therefore you can save via capital gains and spend more than you earn. This excessive lending was

assisted greatly by generally low interest rates - in the US partly due to China's desire to maintain a weak currency and in peripheral Europe due to "higher risk" countries benefiting from interest rate convergence after adopting the euro.

The ensuing global financial crisis could have been a lot worse had it not been for the co-ordinated actions of authorities globally to provide unprecedented levels of fiscal and monetary stimulus. We are concerned that unsustainable private sector stimulus has been replaced by unsustainable public sector stimulus.

² Source: IMF (2009 GDP at PPP)

Where we are today

Much of the world's economy ventures into this decade in a fragile, overly-indebted state with excess capacity and demographic problems.

The US (20.4%² of global economy) is just about to reach (and then raise) its legislated ceiling for government debt (\$14.3trn).

This is just over 100% of 2009 GDP and excludes enormous US liabilities for unfunded future medical welfare benefits. US states such as Illinois and California, which have economies larger than most countries, are looking in

even weaker financial health. The US 2010 average unemployment rate of 9.7% is the tied highest annual rate since records began in 1948 and there are few signs of material job creation (see US credit cycle graph on the following page).

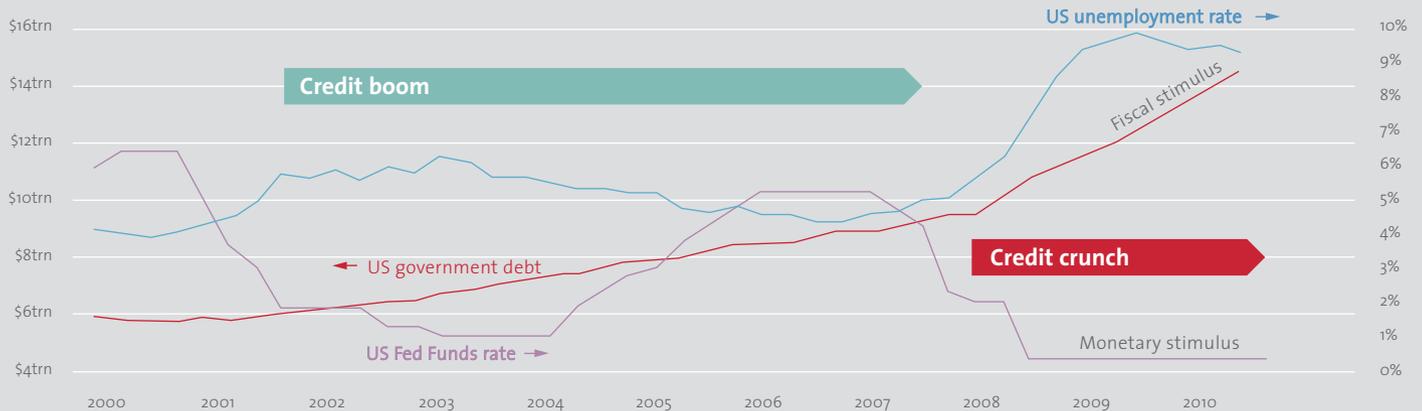
Europe (18.2%)² is structurally weak, with a powerful, surplus-producing Germany not offsetting very weak peripheral countries, low-growth central Europe and problematic banks. There seems to be a high likelihood that Greece defaults (probably as a "debt restructure") and Ireland and Portugal may not be far behind. Austerity is the future for much of the region.

"Much of the world's economy ventures into this decade in an overly-indebted state with excess capacity."

Past decade: Volatility and some new extreme highs

| THE LAST DECADE | FIRST 8.5 YEARS | NEXT 9 MONTHS | FINAL 1.5 YEARS | ENTIRE DECADE | DECADE'S ANNUAL RATE | 31 DEC 2010 |
|--|-----------------|---------------|-----------------|---------------|----------------------|---------------|
| S&P500 (total returns in USD) | 11% | -36% | 64% | 15% | 1% | |
| FTSE/JSE All Share (total returns in USD) | 351% | -44% | 137% | 503% | 20% | All-time high |
| MSCI Emerging Markets (total returns in USD) | 226% | -7% | 14% | 245% | 13% | |
| Copper price | 385% | -54% | 141% | 439% | 18% | All-time high |
| Gold price | 239% | -1% | 53% | 412% | 18% | All-time high |
| Oil price | 494% | -67% | 103% | 298% | 15% | |
| Platinum price | 233% | -46% | 56% | 184% | 11% | |
| Rand/dollar exchange rate | -3% | -18% | 44% | 14% | 1% | |

An extreme US credit cycle



Source: INet

Japan (6%)² has been sluggish and over-indebted for years and faces negative demographic trends, including an ageing and now declining population.

The remaining (55.4%)² of the world economy appears to be in generally good shape, especially the emerging economies (46.2%)² - many with strong balance sheets, favourable demographics and strong growth (notably China, at 12.6% of the global economy).² Their prospects are, however, strongly linked to the sluggish developed world through capital flows and trade and to inflationary pressures that are mounting. Many financial assets in these regions are, however, pricing in excessive optimism about the future and capital misallocation may be causing longer-term problems.

The coming years

Unfortunately, the stimulus must end and be reversed, as even governments and central banks do not have infinite resources. This is a huge global economic headwind.

Ending the stimulus means: raising interest rates, stopping the liquidity flood (quantitative easing) and reducing temporary tax concessions, welfare subsidies and government investment programs.

Reversing the stimulus then means: removing liquidity (repurchase or repayment of bonds held by central banks), raising taxes and reducing government expenditure and investment.

Government austerity means real pain

In many cases, citizens will object aggressively to the fiscal reversals. They will not often realise it, but they will be advocating transferring economic pain from themselves to future generations or, in some cases, to other parts of their population.

They will face such unpalatable prospects as: the raising of state pension retirement age (e.g. to 62 from 60 in France, a new link to life expectancy in the UK), reductions in benefits (e.g. unemployment insurance extensions in the US, the NHS in the UK), direct job cuts in the public sector (e.g. austerity cuts in the UK, cuts to the military in the US), higher taxes (e.g. the new 20% VAT rate in the UK and the possibility of VAT introduction in the US), new temporary taxes (e.g. the UK bank bonus tax, the temporary sales taxes in Hungary and Croatia), reductions in tax concessions (e.g. potentially the removal of mortgage interest deductions in the US), better, wider tax collection (e.g. in Greece), wage freezes or reductions (e.g. in Greece), the removal of subsidies (e.g. the raising of tuition fees in the UK) and so on.

In addition, corporate product and service providers to governments will see orders reduced and business shrink and government employees themselves will see cutbacks.

The important point is that government spending and debt is ultimately, directly paid for by a country's citizens themselves - it can be deferred but not avoided.

² Source: IMF (2009 GDP at PPP)

Stimulus addiction and withdrawal

South Africa is not like other emerging markets

South Africa is deemed an emerging market and has therefore received capital inflows as huge volumes of developed market funds seek out better yields and growth prospects than at home. This has caused an unrealistically strong currency and buoyant asset markets.

This is good for consumers of imports and those, such as government, investing in capital goods from overseas. It is good for those raising capital at historically low cost. It is, however, very bad for our manufacturing sector - which must compete with cheap imports and struggle to remain competitive in export markets. In particular too, our mining companies' revenues in rands are lowered.

Certain sectors of the South African equity market are overvalued as a result of this foreign investment, particularly consumer-focused companies, such as retailers. We are concerned that the ending and reversal of developed economy stimulus may cause a rapid and destabilising outflow of capital from the country. Historically, this has meant a weakening of the currency and temporary inflation increases, which are met with higher interest rates.

We worry too that the new emerging market investors may begin to better understand the prospects of different emerging market countries with closer scrutiny and reverse their decision to see South Africa in the same positive light as other faster growing countries such as China, Brazil, Turkey, Indonesia, Russia and India. South Africa often exhibits the worst structural problems of both "worlds".

Not unlike many developed countries, South Africa has a low savings rate and a large current account deficit, excess capacity and very high unemployment as well as a high cost, inflexible labour market.

In common with developing countries South Africa has: very poor health and education systems for the majority, very high income and wealth inequality and ineffective government delivery of services as promised to its voters. In particular, South Africa has a very narrow and shrinking tax base (just over 200 000 people pay 51% of personal tax) and huge and expanding voter welfare commitments. It has a vast pool of unskilled, young citizens in an economy that is shedding jobs.

Unfortunately, these characteristics structurally lower the long-term growth potential of the country's economy.

"We are concerned that the ending and reversal of the developed economy stimulus may cause a rapid outflow of capital from the country."

This is despite South Africa's positives, including resources endowment, tourism potential, proximity to fast-growing African economies, a world class financial system and corporate governance framework, a relatively stable political situation and

prudent fiscal and monetary management by government.

Lower return expectations

In summary, stimulus "withdrawal symptoms" in the developed world will be painful in the years to come. However, the growth will continue in emerging markets but it will perhaps be less than market prices suggest. South Africa is associated with high growth developing economies but, for unique structural reasons, does not face as rosy a medium-term outlook.

Our sense is that there will not necessarily be any large correction or a crisis but that prospective returns from the South African financial markets will be pedestrian relative to the 2010 decade. We start the new decade with very high asset and currency price levels.

Kagiso Asset Management Funds

| PERFORMANCE TO 31 DECEMBER 2010 | 1 YEAR | 3 YEARS ¹ | 5 YEARS ¹ | SINCE LAUNCH ¹ | LAUNCH | TER ² |
|---|--------|----------------------|----------------------|---------------------------|-----------|------------------|
| COLLECTIVE INVESTMENT SCHEME FUNDS³ | | | | | | |
| Equity Alpha Fund | 22.4% | 9.0% | 18.0% | 25.8% | 26-Apr-04 | 1.3% |
| Domestic Equity General Funds Mean | 18.3% | 5.2% | 12.6% | 18.9% | | |
| Outperformance | 4.1% | 3.7% | 5.4% | 6.9% | | |
| Islamic Equity Fund | 22.2% | | | 29.4% | 13-Jul-09 | 1.6% |
| Domestic Equity General Funds Mean | 18.3% | | | 26.2% | | |
| Outperformance | 3.9% | | | 3.2% | | |
| Protector Fund | 9.8% | 6.6% | 10.7% | 12.9% | 11-Dec-02 | 3.0% |
| CPI + 5% ⁴ | 8.9% | 12.2% | 12.0% | 11.1% | | |
| Outperformance | 0.9% | (5.6%) | (1.3%) | 1.8% | | |
| INSTITUTIONAL FUNDS⁵ | | | | | | |
| Managed Equity Fund | 22.6% | 9.9% | | 15.8% | 1-Sep-06 | n/a |
| FTSE/JSE SWIX All Share Index | 20.9% | 7.1% | | 13.2% | | |
| Outperformance | 1.7% | 2.8% | | 2.6% | | |
| Core Equity Fund | 21.0% | 9.0% | 16.3% | 22.1% | 1-Nov-04 | n/a |
| FTSE/JSE SWIX All Share Index | 20.9% | 7.1% | 15.1% | 20.9% | | |
| Outperformance | 0.1% | 1.8% | 1.2% | 1.2% | | |
| Balanced Fund | 17.4% | 10.6% | | 9.4% | 1-May-07 | n/a |
| Peer Median ⁶ | 18.3% | 9.8% | | 8.6% | | |
| Outperformance | (0.8%) | 0.8% | | 0.8% | | |
| Bond Fund | 14.0% | 10.0% | | 8.6% | 1-May-07 | n/a |
| BESA All Bond Index | 15.0% | 10.0% | | 8.4% | | |
| Outperformance | (1.0%) | 0.0% | | 0.2% | | |
| Money Market Fund | 7.3% | 9.6% | 9.2% | 8.8% | 1-Jan-04 | n/a |
| Alexander Forbes STeFI Composite Index | 6.9% | 9.2% | 8.9% | 8.5% | | |
| Outperformance | 0.3% | 0.4% | 0.3% | 0.3% | | |

¹Annualised. ²TER (total expense ratio) = % of average NAV of portfolio incurred as charges, levies and fees in the management of portfolio for the last rolling 12-month period, except for figure 3.0%, which is at end September 2010. ³Source: Morningstar. Net of all costs incurred within the fund. ⁴CPI lagged by 1 month. ⁵Source: Kagiso Asset Management. Gross of management fees.

⁶Median return of Alexander Forbes SA Manager Watch: BIV Survey.

Tips for taking better pinhole camera images

Making the camera light-tight

It's important to ensure that the camera is light-tight. Once you've made the camera, take off the back cover and hold it up to the light. Look inside the camera to see if there is any light shining through. The tiniest dot will expose your film. Therefore seal off any light sources with either black tape or paper.

Scoring the paper

Before cutting out the camera score the paper on the fold marks. To do this you can use an old ballpoint pen, one with no ink is preferable or a blunt knife and a ruler. Pushing hard draw a line along the fold line. Later you'll fold along the scored line giving you an accurate and clean fold.

Film

The images in this newsletter were taken with Fujicolour 100 and 200 ASA film. Both slide and negative film was used. The exposures are described under the images.

Keeping the camera still

To get sharper images, place the camera on a stable surface like a table or tripod.

Winding on the film

Some light may creep into the camera. This may not be a problem as it adds to the charm of the image. It is recommended that the film frame is wound into position just before taking an image and wound off immediately after taking the image.

Bracketing

Try using different times to expose your film. Without moving your camera, take an image by exposing for one second, then two seconds, four seconds, eight seconds, 16 seconds, 30 seconds, one minute, two minutes and four minutes. This will give you a variety of exposures.



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