

The higher than normal cash component in the Optimal Fund

The Optimal Fund invests in a portfolio of shares and limits stockmarket risk by selling stock index futures. Because of the margin requirement against the futures contracts, the Fund can never have 100% in shares. The Fund typically has a 5% cash holding, 10% cash on margin (against the futures contracts) and 85% invested in gross shares (on a net basis market neutral applying a beta-adjusted formula). As a result of the effective 15% cash holding, the Fund will earn a component of its return in normal interest. In other words, on 85% of the Fund, the return is the implicit interest return in the pricing of the futures contracts plus/minus an equity alpha (out/underperformance) and on 15% of the Fund, it will earn a normal interest return (approximating call rates).

There will be times when the 85% invested in gross shares could be slightly lower (but never below 75%) depending on the pricing of the futures contracts. For example, should the futures contracts be temporarily trading below 'fair value' and hence capturing an inferior interest return for the period of the contract, it may not make sense to buy shares and sell the futures against them and lock in that inferior return. In this situation, one would wait for the contracts to return to 'fair value' before buying the shares and selling the futures. During periods like this, the normal interest return component of the Fund could be slightly higher than the 15% referred to above and could at times approach a maximum of 25%.

Commentary by Stephen Mildenhall, Chief Investment Officer

The maximum drawdown figures as reflected on the fund fact sheets

In April 2003, Allan Gray changed the way in which it calculated the maximum drawdown figures. The calculation is now more in line with that of our global asset management partner, Orbis. The difference mainly arose from the number that was reflected for the FTSE/JSE ALSI drawdown in April this year as -27.7. This would have been better represented as a lower figure in order for it to tie up to what could be seen on the graph on the fund fact sheet as being the biggest general downtrend in the performance. In other words, even though there might be upward spikes in-between, the measurement extends until the point where the general trend changed to that of one in the upward direction. To do this, the calculation had to be changed to run off the cumulative performance as opposed to the fund prices.

In summary therefore, the drawdown is the maximum decline in the investment performance (including income) over any period. When the changes were made, the FTSE/JSE ALSI drawdown changed from -27.7 to -34.4 and the Stable Fund from -2.8 to -2.3. This also stripped out the effect that any distribution dropping out of the price might have had, which might have overstated the decline. The numbers will now always be directly interpretable from the graphs with the current method of calculation.

Commentary by Julie Campbell, Head Performance Analyst