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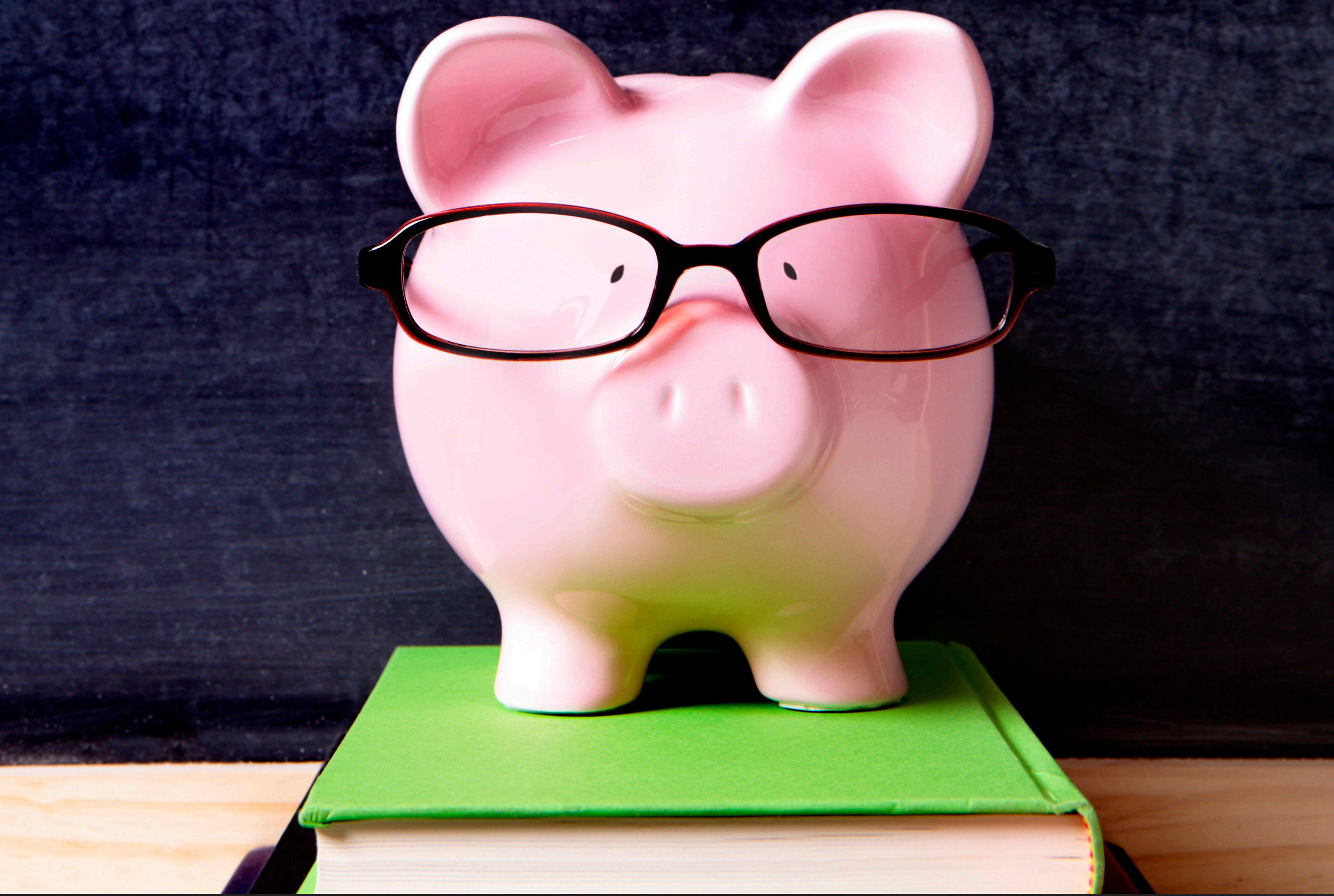
UNIT TRUSTS 101

HOW DOES A UNIT TRUST FUND WORK?



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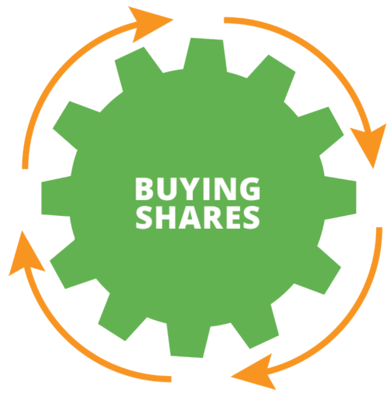
HOW DOES A UNIT TRUST FUND WORK?

A unit trust pools the money of many people and invests it in shares, bonds, money market instruments and other investments. This pool is then divided into identical units (participatory interest), each unit containing the same proportion of the assets in the portfolio.

Unit trusts set a minimum investment amount – investors can choose to invest a lump sum or a monthly debit order. Lump sums typically start at R1 000 and minimum monthly debit orders at R100 per month. Investors share in the fund's gains, losses, income and expenses on a proportional basis.

Unit trust management companies are required to operate their investments within certain requirements or mandates, laid down by the Association of Investments and Savings SA (ASISA) and the Financial Services Board (FSB). The primary purpose of these mandate requirements is to protect the investments of unit trust holders.

Given that each unit (or participatory interest) is exactly equal, and that the sum of all units in the particular unit trust equals the value of the portfolio, it follows that the value of one unit can be easily calculated by dividing the value of the portfolio by the number of units in issue. The net asset value of a portfolio of the market value of the investments in the portfolio less any liabilities due by the fund (such as administration costs not yet paid).



The underlying assets in a Unit Trust fund are made up of:

- cash or money market instruments,
- shares, gold bullion,
- listed property,
- listed offshore shares,
- local government bonds
- equity derivative products are used to protect the downside.

SIMPLE AND STRAIGHTFORWARD

The popularity of unit trusts in South Africa can be attributed to the simplicity of the product structure, cost transparency, the ease of valuing unit trust investments, and the simplicity of buying into and selling out of these products. The industry has created systems which make it very straightforward for investors to buy unit trusts, either through a financial advisor, directly via a management company or even online. Convenient unit trust product features include monthly debit order facilities and reinvestment of income.

FEES

The manager of the unit trust (the management company) is entitled to charge certain fees for the services rendered in administrating the fund's affairs and managing the portfolio. A number of types of fees are used, but the most common are initial charges and annual service fees. Initial charges, as the term implies, are a once-off fee applied when units are purchased. Annual service fees (which might also be called annual management fees) are the fees charged by the management company on an ongoing basis for portfolio management and administration.

Other costs and charges may be applied by a fund manager in addition to initial fees and annual management fees.

RETURN ON INVESTMENT

The return to the investor from his or her investment in the unit trust comes from two elements: capital growth and income. Certain kinds of assets, such as shares and property, are subject to changes in market value, leading to capital gains and capital losses. Other assets like cash only earn income. If you deposit R1 000 in a savings account, the "capital" (the R1 000) is fixed, and you earn interest. But if you buy a flat and you rent it out, you earn income (rentals), and at the same time, the value of the property may rise (a capital gain).

When it comes to unit trusts, capital growth refers to an increase in the price of units which occurs as the values of underlying investments rise. (Of course, these can also go down, which would lead to capital losses.)

The income from a unit trust comes from two main sources: dividends and interest. Dividends are paid by shares, and interest is earned on the cash held in the portfolio. (Although some fund managers aim to be fully invested, the daily creation and redemption of units within a unit trust means the fund must always have some cash on hand.)

*Source: Profile's Unit Trusts & Collective Investments

DISTRIBUTIONS

Investors in unit trusts can usually elect to either have the income paid to them on a periodic basis (quarterly or semi-annually) or to have the income automatically reinvested. Not all collective investment schemes offer these choices. Property unit trusts, for example, usually do not offer automatic reinvestment, and some funds absorb income into the portfolio and do not offer distribution of income to unitholders.

When income is automatically reinvested, the management company applies the distribution due to a unitholder to the purchase of more units. Capital gains, in other words, mean an increase in the unit price, while the reinvestment of distributions means more units in the investor's account.

CAPITAL GAINS TAX

A capital gain is, literally, the increase in the value of "capital" due to higher market prices. Some assets produce both income and capital growth (like shares, which go up in price and pay dividends); others only one or the other (like Krugerrands, which do not generate income but may provide capital growth if the gold price goes up; and like fixed deposits, which do not offer capital growth, but generate income in the form of interest).

From October 2007 (by the introduction section 9c of the Income Tax Act), JSE limited equity shares held more than three years are deemed to be held as capital and are subject to Capital Gains Tax (CGT) rather than income tax.

Under South African Capital Gains Tax legislation, the capital gains on unit trusts are taxable in the hands of the investor when he or she sells the investment. (The manager of the collective investment scheme is exempt from CGT in respect of the operations of the fund, allowing the manager to buy and sell shared within the portfolio without being liable for CGT.) For an individual, 40% of the capital gain must be added to the taxpayer's income.

YIELD

The yield of a unit trust is a measurement of the income distribution paid to investors by a fund as a percentage of the unit price. (Unlike a fixed deposit account, where the advertised rate of interest tells the investor what the bank will pay, for example, at the end of the month, the published yield on a unit trust is a purely historical indication – it is no guarantee of the future yield.)

*Source: Profile's Unit Trusts & Collective Investments

TAX ON DISTRIBUTIONS

Distributions made by unit trusts are taxed in the hands of the investor. An investor is liable for tax on distributions whether the distributions are physically paid out to the investor or automatically reinvested on behalf of the investor.

Different rules apply to tax on interest and dividends. The income tax certificate issued by the fund manager to the investor at year-end will show the respective amounts of interest and dividends that make up the total distributions that accrued to the investor during the tax year.

Dividends from equities (whether shares are held directly or via unit trusts) are taxed in the hands of individual investors at a flat rate of 20%. (The fund itself does not pay tax on dividends it receives from investors.) Tax on dividends, introduced in 2012, is a withholding tax, which means the fund manager deducts the tax and remits it to SARS on behalf of the investor (i.e. the amount received by the investor is net of tax).

Interest paid to an investor in a unit trust is taxed as part of the individual's income. For individuals under 65 years of age, the first R23 800 of interest received is exempt (R34 500 for individuals over 65), thereafter interest is taxed at the individual's marginal rate.

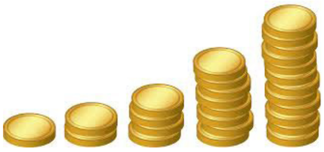
MONTHLY DEBIT ORDERS

One of the convenient features taken for granted by unit trust investors is the monthly debit order facility offered by nearly all CIS managers. A bank authority signed by the investor allows the CIS manager or Link Investment Service Provider (LISP) to deduct a fixed monthly amount, creating a "contractual saving" for the investor.

Unit trusts investments made on a monthly debit order basis enjoy the benefit of what is called "rand cost averaging". Using the debit order system, an investor buys unit trusts units by investing the same amount of money every month regardless of the market price. Rand cost averaging allows the investor to avoid guessing whether the market is going up or down. The advantage of this method is that your rand buys more units when the prices are declining.

Share market prices are typically cyclical in nature. Although over the long-term they go up more than they go down, share markets usually advance in a series of rushes and retreats. While some market professionals try to use the "dips" to buy while prices are down, it is notoriously difficult to pick market low points.

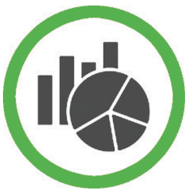
*Source: Profile's Unit Trusts & Collective Investments



THE POWER OF COMPOUNDING

Both lump sum and debit order investments in unit trusts can benefit from the power of compounding. Nearly all South African unit trusts offer a facility whereby income distributions can be automatically reinvested. If an investor elects to automatically reinvest, instead of paying dividends and interest into the investor's bank account, the CIS Manager uses the dividends and interest to buy more units for the investor. This creates what is known as "compound growth", a simple multiplier effect which can dramatically enhance investment returns.

"Compound interest" refers to the interest earned on interest that was earned earlier and credited to the capital amount. For example, if you deposit R10 00 in a bank account at 10% and interest is calculated annually, your balance will be R1 100 at the end of the first year and R1 210 at the end of the second year. That extra R10, which was earned on the interest from the first year, is the result of compound interest ("interest on interest"). Interest can also be compounded on a monthly, quarterly, half-yearly or another basis.



ASSET ALLOCATION

Investments are conventionally divided into five asset classes: cash, bonds, equities, property and exotics. The last category includes collectables such as art, jewellery, and rare stamps, and the managers of collective investment schemes are not permitted to invest in them. The different characteristics of the four main assets make them suitable for different investment objectives, and have a direct impact on the characteristics of the collective investment schemes which invest in them, in broad overview:

- Equities (shares in companies) are generally considered long-term investments with a relatively high degree of risk, although opportunities for short and medium-term investment do arise in the stock market from time to time.
- Bonds (long-term debt instruments) are considered medium to long-term investments and also carry a relatively high degree of risk.
- Property is considered a long-term investment with a relatively low level of risk.
- Cash (which includes things like money market investments and fixed deposits) is considered a short-term investment with a low-risk level.

*Source: Profile's Unit Trusts & Collective Investments

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MANAGEMENT COMPANY
The portfolios are owned by Novare CIS (RF) (Pty) Limited (Novare CIS) Registration No.2013/191159/07, an authorized Management Company registered according to the Collective Investment Schemes Control Act (CISCA) and regulated by the Financial Services Board of South Africa. Contact details: P.O. Box 4742, Tyger Valley, 7736, South Africa. Call Centre: 0800 668 273 (0800 Novare). Email: clientservice@novare.co.za. Website: www.nova-re.com. First Rand Bank Limited Registration No.1929/001225/06 is the appointed trustee, contact number: 011 282 8000. PricewaterhouseCoopers is the auditor for the portfolios. Maitland is the fund administrator of the portfolios. Risk management of the portfolios is done by Novare CIS. Should you have any queries or complaints please contact: Novare CIS on 0800668273 (0800novare) or via email clientservice@novare.com. Directors: Ms R Miles, Mr DA Roper, Mr L de Wit, Mr GL Carter and Mr JF Basson.

INVESTMENT MANAGER
Novare Investments (Pty) Limited (the 'Investment Manager'), registration no: 2000/018539/07, incorporated under the laws of South Africa, is an authorised financial services provider (FSP 757) under the Financial Advisory and Intermediary Services Act 37 of 2002 and has been appointed by Novare CIS as the Investment Manager of the portfolio. Contact details: P.O. Box 4742, Tyger Valley, 7736, South Africa. Telephone 021 914 7730 Website: www.novare.com The Investment Manager is a member of the Association for Savings and Investment South Africa. Additional information on the proposed investment is available on the Investment Manager's website at www.novare.com

DISCLAIMER
Collective Investments are generally medium to long term investments. Actual investment performance will differ based on the initial fees applicable, the actual investment date, the date of reinvestment and dividend withholding tax. Novare CIS facilitates the issue and sale of the participatory interest in the portfolio. Novare CIS does not provide any guarantee in respect of capital or the return of a portfolio. The value of participatory interests may go down as well as up and past performance is not necessarily an indication of future performance. Collective Investments Schemes trade at ruling prices and can engage in borrowing and scrip lending. Commentary or any forecasts contained in this document are not guaranteed to occur. Novare CIS has the right to close the portfolio to new investors in order to manage it more efficiently in accordance with its mandate. The higher TER does not necessarily imply a poor return, nor does a low TER imply a good return. The current TER cannot be regarded as an indication of future TER's. Novare Holdings (Pty) Ltd has both a Conflict of Interest (COI) and a Treating Customers Fairly (TCF) Policy which respectively outlines the manner in which conflicts of interest are managed and customers are treated fairly, copies of the COI and TCF Policies are available on request. Novare CIS's schedule of fees and charges is available on request. Prices are available on all CIS information websites. The portfolios were established as a Collective Investment Schemes , all information prior was in an unregulated environment. The portfolios will not change its investment strategy or investment policy without prior approval from the Financial Services Board and investors. The ballot procedure as indicated in CISCA will be followed. Counterparty exposure is introduced in the portfolio through the use of a prime broker. The level of counterparty exposure is restricted to funds that are administered by Novare Capital (Pty) Ltd and the respective prime brokers of the underlying portfolio. The liquidity risk management policy is available on request, and covers all repurchase and redemption restrictions, both in normal and in exceptional circumstances. Quarterly reports will be distributed to clients via electronic communication, a month following quarter end. Annual reports will be made available upon request. Nothing in this document will be considered to state or imply that the Funds are suitable for a particular type of investor unless specifically indicated as such. The information contained in this report is provided in good faith and has been derived from sources believed to be reliable and accurate. However, no representation or warranty, express or implied, is made in relation to the accuracy or completeness of this information. The Financial Services Board (FSB) has officially taken up its new mandate as the Financial Sector Conduct Authority (FSCA), effective 1 April 2018. This marks the formal implementation of the Twin Peaks model of financial sector regulation, as envisaged in the Financial Sector Regulation Act 2017 (FSRA). The FSB will henceforth be known as the FSCA.

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